JULY 1958

The Mortgage Banker

MORTGAGE BANKERS ASSOCIATION OF AMERICA
MBA
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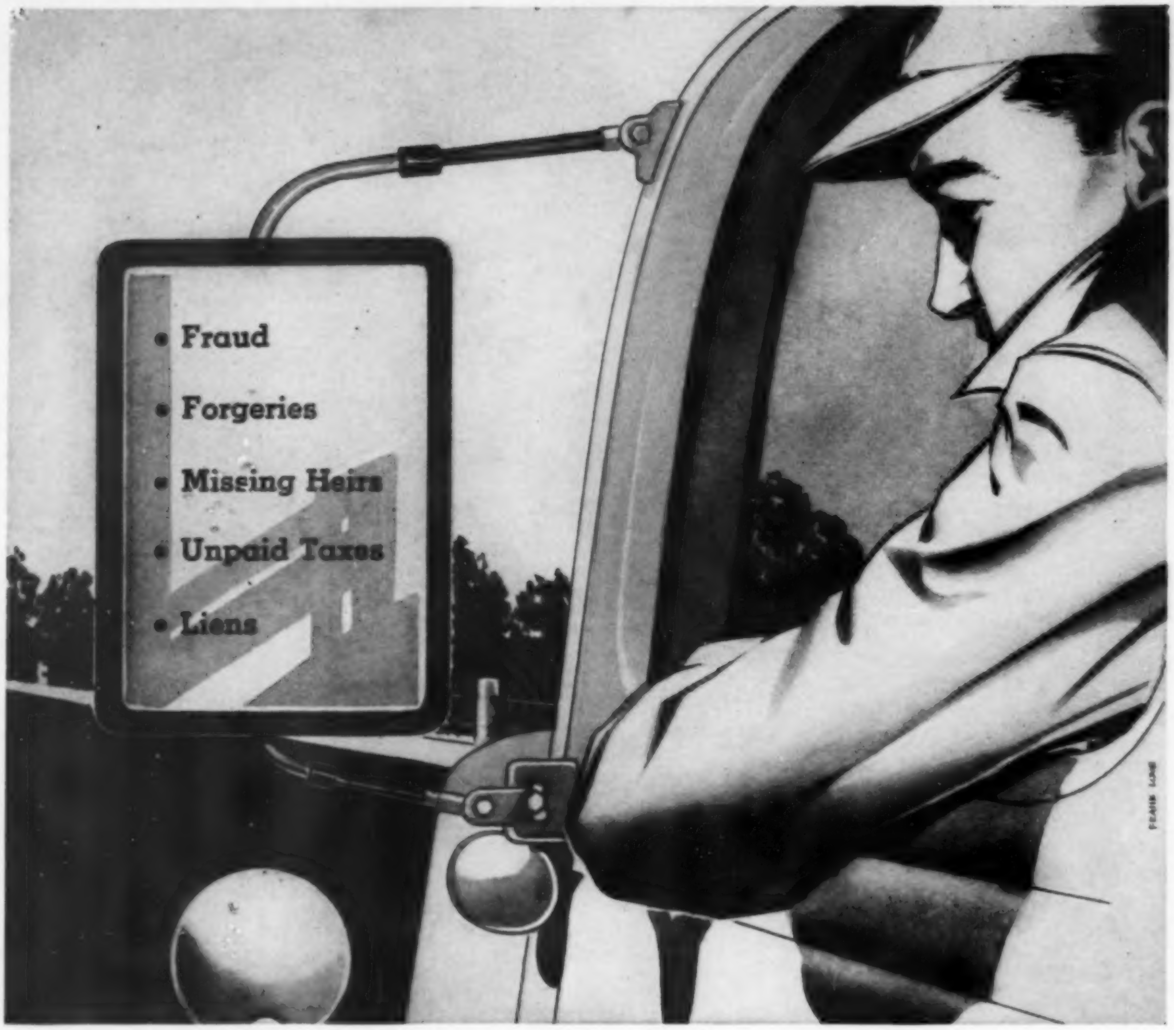
in this issue — BUSINESS AHEAD IN THE DECADE OF THE SIXTIES ★ THE OPERATION OF BRANCHES FOR MORTGAGE COMPANIES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MBA 1958 Calendar

July 27-August 2, School of Mortgage Banking, Course I, Stanford University, Stanford, California

August 3-9, School of Mortgage Banking, Course II, Stanford University, Stanford, California

November 3-6, 45th Annual Convention, Conrad Hilton Hotel, Chicago

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» VACANCIES FEW: Strong demand for rental units financed under FHA is evident with only 2.9 per cent of all available apartments vacant.

The 1958 vacancy rate of 2.9 per cent, although a little higher than the 2.4 per cent reported for March 31, 1957, was below the rates for the three preceding years, which were: 1956, 3.2 per cent; 1955, 4.4 per cent; 1954, 3.5 per cent.

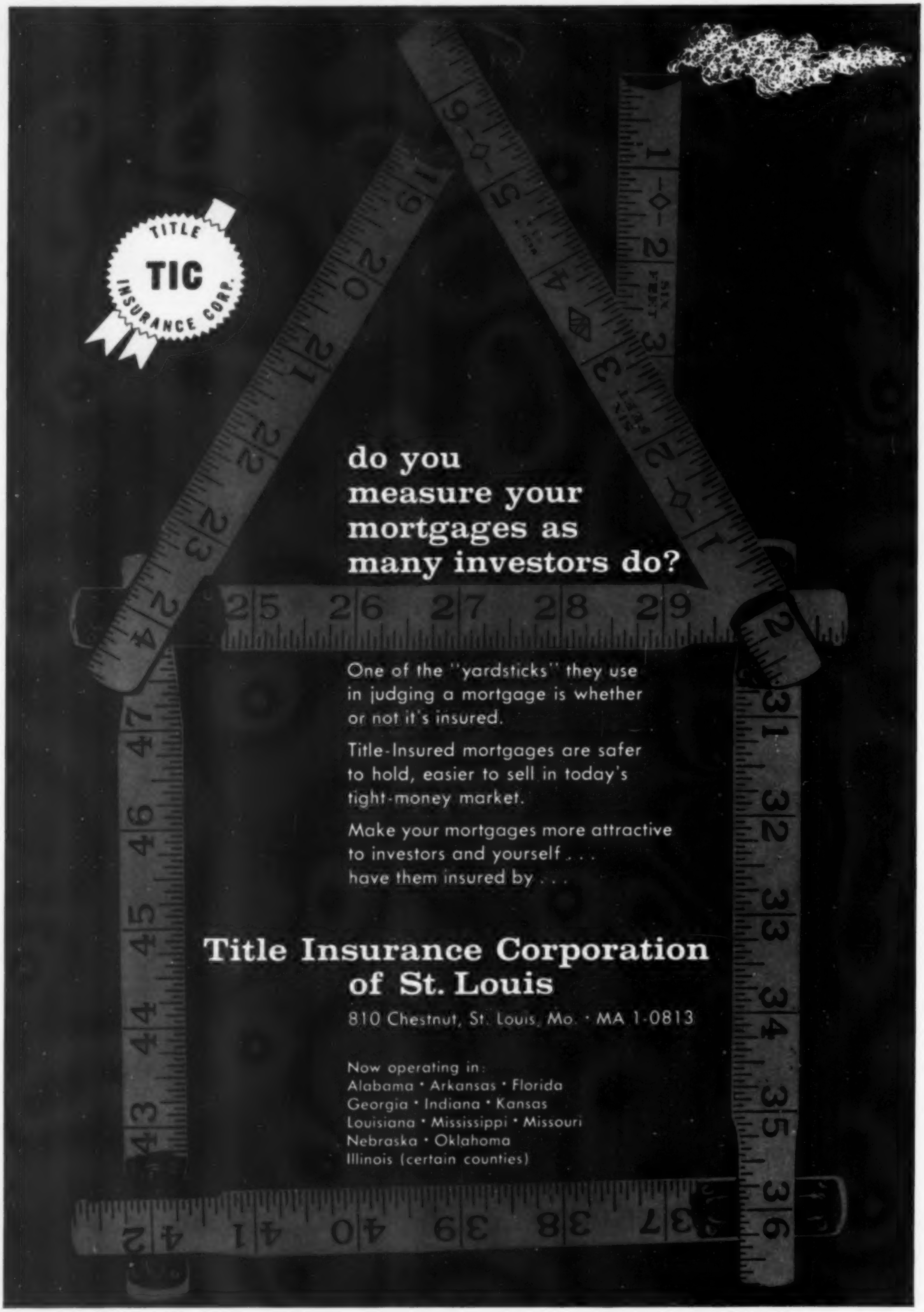
The 1958 analysis covered more than 460,000 dwelling units in rental projects located in all parts of the United States and in Alaska, Hawaii, and Puerto Rico.

The rate of change in the vacancy rate from 1957 to 1958 varied considerably in different parts of the country. The northeastern area, which includes the large concentration of rental units in metropolitan New York, reported the lowest vacancy rate of any section—0.7 per cent, compared with 0.5 per cent last year. In the southeastern States the 1958 vacancy rate of 3.5 per cent was below the 4.5 per cent reported for 1957. The highest 1958 rate—6.5 per cent—was reported in the southwest.

Vacancy ratios in the individual FHA insuring office jurisdictions ranged from 1 per cent or less in nine jurisdictions—including such major centers as Boston, New York, Newark, and Chicago—to over 21 per cent in Alaska, nearly 20 per cent in northern Louisiana, and 17 per cent in Montana.

The largest increases were reported for Alaska, Montana, and Idaho, while the greatest decreases were reported for southern Louisiana, South Carolina, Colorado, and Kentucky.

The vacancy ratios for individual jurisdictions do not necessarily indicate the general vacancy situation.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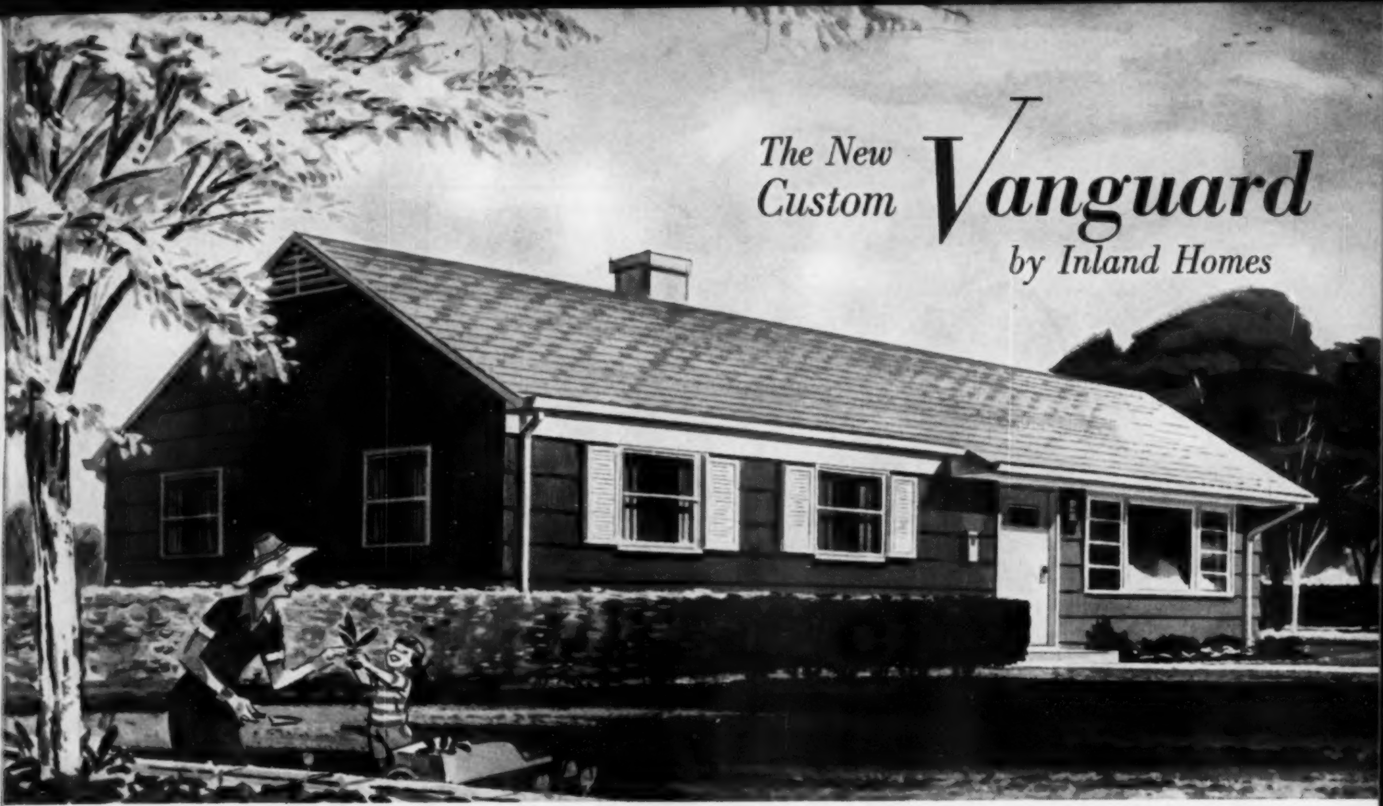

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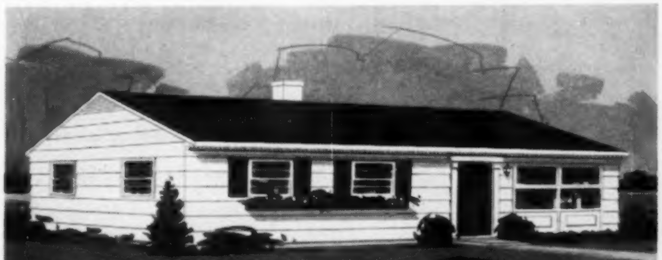

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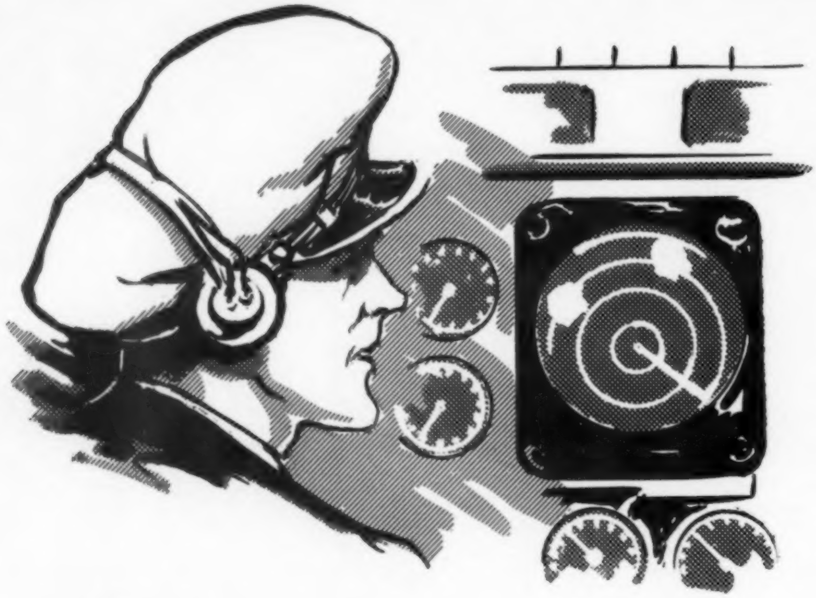

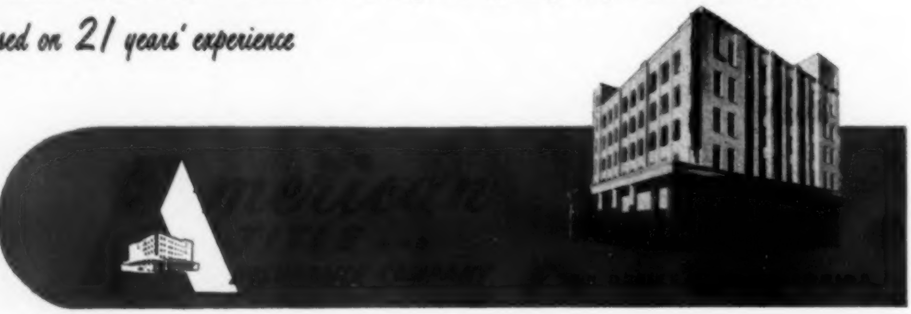

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BUSINESS CYCLE HAS BEEN TAMED

Its teeth have been pulled but it has not been eliminated

Make no mistake about it, says Mr. Rodgers, the business cycle has been tamed. "While it is impossible to eliminate it—as some people are demanding—its teeth have been pulled. . . . This is a recession and, as of now, it is inconceivable that it could degenerate into an old fashioned depression. . . . On the basis of present conditions and outlook, it seems that the downward trend of business should come to an end sometime in the early summer. Business activity will then probably remain at a low level until late in the fall, when seasonal factors, the end of inventory liquidation, increased money supply, increased monetary ease, increased government spending, and the passage of time should have us on our way again—but a repetition of what happened in 1950 or 1955 cannot be expected."

MEASURED by the business levels of 1955-56, we are suffering a recession; but, after our greatest boom, such a recession was inevitable. Moreover, measured by the levels of most past years, we are not doing too badly, even now, in most lines. Unfortunately, the high wartime and postwar levels of business activity have caused too many people to lose perspective. As a result, they expect champagne every day! If the indexes aren't 25 to 50 per cent higher than the past year—whatever the base year may be—they become very gloomy and expect the worst. In fact, they think business activity ought to be like the Kentucky Bishop who was introduced by his local preacher as a "great orator who never falls below his **average,** and usually goes above it"!

This boom-forever philosophy underlies most of the inflationary cures proposed for the slowing up in business activity. Some of these proposals would no doubt be highly effective; but it should be kept in mind that the more effective such a cure, the more dangerous from the longer-pull standpoint, as the extent to which it postpones the correction of unsound conditions is the measure of its effectiveness.

Economic maladjustments cannot be postponed forever. There is no limbo of forgotten things in economic affairs. Correction of maladjustments is a necessary feature of an economy as fearfully complex as ours. They can be made by readjustments, as in 1948-49 and 1953-54, or, by recessions, as at present.

Happily, the traditional "boom and bust" pattern of American business has not been in evidence since the end of World War II. Since then, there have been three distinct periods of boom, but no depressions. Instead of depressions, there have been two distinct periods of "rolling readjustment" — 1948-49 and 1953-54 — in which some industries declined while others continued to boom. Moreover, in each case, the overall readjustment and decline was so mild, that it did not qualify as a recession, much less a depression.

But now, the more serious decline in business activity which started

By **RAYMOND RODGERS**

Professor of Banking, New York University Graduate School of Business Administration, before Illinois Bankers Association Convention, Chicago

after Christmas 1956, is causing some people to fear that this is the traditional postwar depression even though quite delayed in arriving. If, by chance, there are any who think that, perish the thought. This is a **recession** and, as of now, it is inconceivable that it could degenerate into an old-fashioned depression.

Make no mistake about it—the business cycle has been tamed. While it is impossible to eliminate it—as some people are demanding—its teeth have been pulled.

For example, unemployment, the sorest spot in the economy, is in excess of 5 million, and there are other millions on short work-weeks. But this is a far cry from the 13 million unemployed of 1933, or the 10 million of 1938, with another 5 million of hidden unemployment (or, at least, unproductive employment) on the farms during the '30's. In fact, the unemployment total today is just about the number of people who left the farms since 1950! In addition, it includes many housewives from families where both husband and wife are in the labor force. And there are still many people with two jobs—"moonlighting" has not ended by any means, as most know first-hand.

Or, putting it on a statistical basis, unemployment today is only about 7.5 per cent of a much larger working force, whereas it was close to 20 per cent of the working force in 1938.

But, far more important from an economic standpoint, there are now some 40 per cent more gainfully employed than in the late '30's, so that, relative to those employed, our present unemployment is of considerably less economic significance than the unemployment of the '30's. Moreover, the economic rigors of unemployment today are tempered by unemployment insurance payments, supplemental unemployment benefits and relief payments. In fact, this has reached the point in at least one industry where workers net more from tax-free unemployment payments than from taxable income for part-time work!

These statistics and observations are in nowise intended to condone unemployment. Every man who really wants to work should be able to find a job; and, these days, that should be the case for women also. More-

over, there are real financial hardships for many who are unable to find work. Many do not belong to unions with supplemental unemployment benefits; many have exhausted their unemployment insurance payments (which explains the legislative efforts to extend the time period); many do not have working wives; and many are heavily in debt with monthly payments on mortgages on homes and on instalment financing of durable consumer goods.

Nonetheless, the fact is that there are more than 65 million **employed,** including the armed forces, and purchasing power, as measured by disposable personal income (after taxes), dropped only $4 billion from the all-time peak of $303.3 billion in the third quarter of 1957 to $299.3 billion in the first quarter of 1958. This drop of only a little more than 1 per cent in disposable income, even though a much larger percentage of the working force was unemployed, reflects the beneficial effect of some of the economic safeguards we now have in our economy.

It is important to keep in mind that the current decline is not so much a conventional **cyclical** downswing in business activity as a **new phase** of the postwar economic pattern. The first phase of the postwar economic pattern was characterized by an abnormally high level of business activity necessary to fill the great economic void caused by the subnormal business activity of the long depression of the thirties and the diversion of production to military purposes during World War II. Expansion of non-military production, expansion of military production for the Korean war, and the expansion of production necessary for rearmament and a garrison economy have largely come to an end. In fact, our production capacity has been expanded to the point where we really can have both "guns and butter."

In addition to plant and equipment expansion, the great accumulated demand for automobiles and other consumer durable goods, and for housing has been met. This means that we now have entered a period in which the level of business activity must depend on **current** demand, plus modernization and replacement. This can hardly be over-emphasized,

as too many people have come to look upon the high level of business activity of the great expansion of the postwar period as the normal level of business activity, and to think that it should be maintained at all costs. They feel that, if necessary, all the powers of government, especially heavy government spending and large increases in the money supply should be utilized in a bold, determined program to maintain such levels. But the hard facts are that production capacity throughout American industry is greater than present effective demand. Moreover, the productive capacity of the Free World is greater than ever before, so exports cannot rescue us. This means that we shall have to be satisfied with something less than the boom levels of 1955 and '56. Efforts to maintain such boom levels during the more normal period we have now entered can only result in inflationary pressures, which will cause even more trouble later on.

Capital expenditures are not only under the pressure of over-capacity in most industries, they now have the added pressure of a profit squeeze, as three out of four large corporations reporting recently have shown lower profits. Moreover, although substantial expenditures will be necessary for further automation and, also, to bring the fruits of the heavy research expenditures to our people and the government, capital expenditures on an overall basis have entered a long, cyclical downswing, which will probably last into the early '60's, when growing family formation and the passage of time should cause another upswing.

Inventory reduction has played an important part in the decline in industrial production. Inventory reduction accounted for virtually all of the 1948-49 downturn and almost half of the 1953-54 downswing. Moreover, studies of the National Bureau of Economic Research show that inventory liquidation, **on the average,** accounted for more than half the decline in production in all business contractions since 1918. This is good news, as inventory liquidation is necessarily a temporary weakness. Sooner or later, inventories decline to the point where they must be replenished, and then they become a source of strength.

Debt reduction, likewise, is a temporary phenomenon. This is particularly true of personal debt. Sooner or later, such debt is reduced to the point where it is not so burdensome to the individual or the family. This improves their credit standing and changes the desire to repay to a desire to make new instalment purchases.

Declining exports are, like declining capital expenditures, a fundamental factor in the current decline in business activity. The boom in Europe is coming to an end, the productive capacity of the Free World is greater than ever before, and there is a dollar shortage in many countries, because of the sharp decline in the world price of the raw materials they sell us. In addition, declining business activity has brought great pressure on the United States to reduce imports in several fields. This, of course, is causing repercussions abroad.

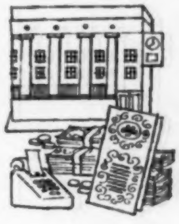
What can the government do to reverse the downward trend in business? As anything and everything that the government does has an effect on business activity, it follows that there are many things that can be done to help reverse the trend. As they are not all equally desirable, especially from the standpoint of inflation and after-effects on the private side of the economy, the more important ones will be briefly surveyed.

A consequential increase in the money supply is, of course, the first thing which comes to mind, as we have a managed money. Moreover, some justification can be found for such an increase, as growth of the money supply has not kept pace with the increase in the physical output of goods and services since the "accord" of March 1951 between the

Federal Reserve and the Treasury. This can be done through reduction in reserve requirements and through open market operations of the Federal Reserve Banks. But such an increase should be done very carefully because it will do more harm than good, as in 1953-54, if over-done.

Lower reserve requirements and permission to count vault cash as part of reserves, as provided in the Fulbright and the Spencer bills now pending, would be the soundest way to accomplish such an increase in the money supply. In the meantime, the apparent Federal Reserve policy to maintain $500 million, or more, "free" reserves will lead to an increase in the money supply and a further moderate reduction in money market rates.

"Government action, Federal Reserve policy, and declining loan demand will still further increase the availability and lower the cost of money in the months ahead. This easier money will, of course, have broad economic consequences. Banks with savings deposits will be aggressive buyers of mortgages. This will not only have a direct favorable effect on home starts, it should enable FNMA to reduce its holdings of some $1.5 billion of VA and FHA mortgages. Thus, easier money should permit a moderate improvement in home starts. However, an all-out housing boom cannot be visualized as the prices of homes are at high levels, local taxes are increasing continuously, and the costs of transportation from the suburbs are likewise mounting, although the service steadily gets worse."



Tax reduction, especially of personal income taxes, is the most potent stimulus the government could give the private sector of the economy. In 1953, when business activity began to turn down, the Administration told the country in positive terms that a tax reduction could be expected in 1954. The stimulus this gave the economy was literally astounding.

But, this time, the Administration is reluctant to use the weapon of tax reduction. The principal reason for this opposition is that a reduction would further increase a deficit which, even without a tax cut, will be very substantial, and thus increase the danger, and the fear, of inflation. That fears on the size of the budget deficit are based on fact is indicated by Secretary Anderson's addition the other day of $4 billion to the amount he expects the government to spend in fiscal 1958-59. With this increase in expenditures, and a probable drop

of $4 billion or more in revenues, the budget deficit in the coming fiscal year may reach $10 or $11 billion **without tax reduction.** As this deficit will, in large part, be financed through the banks, the danger of reviving the forces of inflation by increasing the deficit to cover a tax reduction of $4 or $5 billion is apparent.

The proponents of income tax reduction, nevertheless, argue that it would cost the government less in the long-run to stimulate the economy by lower taxes than by any other method. They maintain that government revenues are not determined by tax **rates,** but by the application of such rates to the income generated in the **economy,** and that a sound reduction in rates might very well eventually result in increased revenues, because of its favorable impact on business activity.

Of course, if by some miracle both expenses and taxes could be cut, the economy would really jump. The heavy burden of the current level of taxes is shown by the studies of the Tax Foundation, which indicate that Federal, state and local taxes, including hidden taxes, take approximately one-third of the income of United States families at average income levels. Anything which would lighten such a burden would certainly have a most favorable effect on the psychology of consumers, who, in the last analysis, hold the key to both business revival and continuing business prosperity.

Large scale government spending will also help revive the economy. But such increased spending takes quite a while to have much effect on the economy, as is evidenced by the Federal road program, of which so much was expected. Plans have to be drawn, rights-of-way have to be acquired, contracts have to be let, and after that it may take as long as a year or even two years for the job to be finished and have its full impact on the economy.

It even takes considerable time to expand defense spending. For example, although defense **orders** for major items have more than doubled from the $2.1 billion of the third quarter of 1957 to the $5.4 billion rate of this quarter, actual national security **spending** this quarter will apparently be less than in that quarter.

In any event, overall government spending is bound to cause a substantial increase in the money supply, especially during the second half of this calendar year. To be specific, the **cash** outflow for fiscal 1958-59, starting July 1, is now estimated at $92.3 billion, while the **cash** intake by the government is put at $82.1 billion, which leaves a deficit of $10.2 billion.

As almost all of this cash deficit will materialize between July 1 and December 31 of this year, and as almost all of it will probably find its way into the commercial banks, a large increase in the money supply seems inevitable.

Government action, Federal Reserve policy, and declining loan demand will still further increase the availability and lower the cost of money in the months ahead. This easier money will, of course, have broad economic consequences.

Banks with savings deposits will be aggressive buyers of mortgages. This will not only have a direct favorable effect on home starts, it should enable FNMA to reduce its holdings of some $1.5 billion of VA and FHA mortgages. Thus, easier money should permit a moderate improvement in home starts. However, an all-out housing boom cannot be visualized as the prices of homes are at high levels, local taxes are increasing continuously, and the costs of transportation from the suburbs are likewise mounting, although the service steadily gets worse.

Military housing and public housing, however, may be expected to increase considerably, which will have a favorable impact on the economy. The easier money conditions will also have a favorable effect on the volume of other public construction. State and local governments may be expected to sell growing amounts of their obligations to finance the construction of all kinds of public works. This expansion should have a marked favorable effect on both employment and business activity toward the end of the year.

As this recital has shown, there are many forces in the economy working for recovery. In addition to those which have been enumerated, the most basic economic force of all—**time**—should be kept in mind. Time is steadily working for recovery, and every day that passes brings us that much closer to the end of the downswing.

Also, there are many more things the government could do which would affect the rate of recovery and future business activity. Only time can tell what actually will be done, as political issues are involved.

Nonetheless, on the basis of present conditions and outlook, it seems that the downward trend of business should come to an end sometime in the early summer. Business activity will then probably remain at a low level until late in the fall, when seasonal factors, the end of inventory liquidation, increased money supply, increased monetary ease, increased government spending, and the passage of time should have us on our way again—but a repetition of what happened in 1950 or 1955 cannot be expected.

We Haven't Been Meeting the
Minimum Demand for Housing

That minimum, say the Dodge experts, is about 1,250,000 units annually and of course we're falling behind that now. Principal reason for the deficiency in the recent past has been lack of funds, a factor which is no longer present. In any event, as far as the Dodge projections go, there is still a great demand for housing in this country but there are also a great many factors affecting the immediate volume ahead.

By **EDWIN W. MAGEE, JR.**
Economist, F. W. Dodge Corporation, at the MBA San Diego Clinic

IT wasn't too long ago that construction was being counted upon to supply a substantial boost to the economy in 1958. Well, so far this year, our Dodge figures on contracts for future construction haven't offered very much to cheer about.

Total construction contracts in January this year were 10 per cent below the same month last year. February contracts again registered a 10 per cent decline from a year ago and in March the figures showed a 12 per cent drop from March '57.

What are the chief soft spots? First of all, industrial building contracts for the first three months were down 46 per cent from the comparable period last year. Commercial buildings are down 11 per cent. Heavy engineering contracts—including public works and utilities are down 12 per cent. And residential contracts are down 8 per cent in value and 5 per cent in the number of units involved. Some signs of encouragement in the residential area showed up in March though with the number of units that month registering a one per cent gain over March of last year.

Construction is definitely being affected by the recession. It is the nation's largest fabricating industry accounting for about 15 per cent of the total output of goods and services of the American economy. Because of its tremendous size, construction activity affects the general business outlook and, in turn, is affected by it. Today, it seems evident that the construction outlook is being dominated by the business outlook.

This is particularly true in the area of home building. Aside from the psychological effects of the recession, there is absolutely no reason why housing starts should be down where they are now—at their lowest level since early 1949.

We feel that the basic demand for housing—at a minimum—is currently in the vicinity of about one and a quarter million units annually. But we haven't been building or selling that many new homes for some time. The chief reason for the decline in housing starts in recent years has been the lack of available funds for government-insured mortgages with their relatively low and inflexible interest rates.

Demand for funds by business and government during the past several years resulted in rising levels of interest rates—to the extent that VA and FHA mortgages became unattractive to lenders.

However, this situation no longer exists. Business spending for new plant and equipment has already fallen off and further cutbacks are expected in the year ahead. As a result, there has been a lessening in the demand for funds and a consequent easing in the money market.

In addition, the Federal Reserve Board during the past six months has switched from an anti-inflationary tight money policy to an anti-recessionary easy money policy. Several times since November 1957, the monetary authorities have permitted a reduction in the discount rate at the Federal Reserve Banks and *twice* they have reduced reserve requirements. Money rates in general have fallen

sharply during this period. All these factors, reflecting an overall decline in the general interest rate level, tend to make the current rates on mortgages—particularly FHA at 5½ per cent and even GI at 4¾ per cent—more attractive to lenders. Additional funds should be forthcoming to the mortgage market—funds which last year and the year before—were finding their way into other areas of the economy.

So the prospects for housing this year are good—except for the effects of the recession. Basic demand is present and ample credit is available. The only uncertain factor is the home buyer. The consumer is now cautious—and to some extent fearful of committing himself on a long-range basis until he feels business conditions are improving. The housing outlook is therefore closely tied in with the general economic situation.

With this in mind, what facts can we establish about the present business situation?

First, we have a genuine recession, somewhat more severe than the other two we have had in the post-war period. There are many millions of people who haven't even noticed this recession, but others are hurting. To the more than five million unemployed, to merchants in unemployment areas, to workers whose salaries have been cut, this is no laughing matter.

Second, this recession developed with surprising speed. Early last fall, there was hardly a businessman or economist who thought that by the end of the year, we would be talking in terms of a recession already underway. Even those of us who expected some business dip in 1958 hardly conceived that it would hit in 1957.

Why did the recession come so much faster than anyone expected? There are probably at least three reasons:

First, we suffered something of a shock to our national confidence when the first Sputnik orbited in October.

Second, President Eisenhower suffered what we now know was a very mild stroke, at the worst possible time.

Both these traumatic experiences influenced the psychological atmosphere in which our economy operates. They probably affected thought leaders, including businessmen, more than they did the general consuming public.

The *third* factor is that along about the same time, a wave of defense economy had gotten underway in Washington. Orders were stretched out or cancelled, and there were some big defense producers who had to scramble to get funds to pay workers when Federal payments were delayed.

While all this was going on, the government, and particularly the Federal Reserve Board, was fighting inflation with policies of ever-tighter money. These policies had already effectively provided the home-building industry with its own private recession as far back as 1956.

But these are primarily reasons for the speed of the drop. There were forces operating long before last fall which gave some clues to a coming drop, and which influenced many of the economists on our annual Dodge outlook panel last October to predict a dip in business at some time in 1958.

For one thing: a decline in business plans for new factory buildings began to show up in our Dodge contract figures as early as a year ago last February. It persisted throughout the year, with few exceptions and prompted us to warn in a publication last June that there might well be downward revisions in business plans for plant and equipment investment.

There were other advance indications as well—the housing decline certainly was one of them.

All this is past, however. Where do we stand now, and what of the future?

As I was putting together these observations, I couldn't help thinking of something I had read about ancient rites of spring which still survive as pageants and games in some European countries. In these pageants, forces of winter, or darkness, combat against forces of spring, or light, for possession of a ball which represents the earth. We could make something of an analogy with our current situation, where downward pressures are battling with upward pressures for possession of the economy. What are these forces, and more important, who's going to win?

Among the evil influences, we would certainly have to put some of those I have already mentioned, because they are still operating:

» The decline in business investment, which is still going on, and which is reflected in such things as construction contracts and sinking business appropriations.

» The drop in auto sales, which has been showing no tendency to improve in recent weeks.

» The low level of housing activity at present.

» These and other downward pressures are reflected in other trends which make for still further downward movement. Among these subsidiary trends are:

a. A drop in steel production, to levels 40 per cent or so below last year.

b. An 11 per cent decline in total industrial production from the peak reached in 1957.

c. A drop in freight car loadings of more than 20 per cent from last year.

» And all these things are reflected in still further downward pressures, including, among others:

a. Increasing unemployment, now about 5.1 million, or 7½ per cent of the labor force, and still showing no tendency to stop rising, if normal seasonal factors are taken into account.

b. Increasing numbers of business failures.

c. A declining average work week, which is now the shortest since 1939.

d. And as a result of all these things, declining weekly earnings of labor.

» Then, way down at the end of the line, as a final result we find that:

A. Total personal income has dropped about 2 per cent since last year's peak.

B. And retail sales are down a little.

Notice that at the end of the line, the percentage declines are quite small. This is natural, in such a sequence. The important thing is that they be *kept* small. If they increase, they could well spark further cutbacks in production, and start the process all over from the beginning.

So much for the forces of evil. How about the good side?

» I would list first among the good factors the lack of panic at practically all levels of the economy. The lack of panic is reflected in several things:

a. The relative stability of the stock market, which has comported itself nobly so far.

b. The stability of the financial structure of the country, which is being conducted in a far more orderly manner than it has at many times of stress in the past.

c. The high level of consumer purchases.

d. The stability of prices.

» Among the good factors, I would also include the inventory situation. This could also be included among the downward pressures, since inventory adjustments certainly helped speed the downturn, but I include it here because this correction should be largely behind us. There are many

analysts who think that businessmen over-corrected in view of the stability of sales, and will have to make the reverse adjustment of adding to inventories soon.

» We still have, basically, a growth economy. Our population is three million more than it was last year, the birth rate is still high, and we still have a pronounced "growth attitude." We are devoting tremendous sums to research and development. We have the national attitude that great things are ahead.

» And then, highly important among the upward forces are specific government programs aimed against recession. Practically all of these programs, incidentally, emphasize construction directly or indirectly. Construction will be their prime mover—and their first beneficiary.

In addition to government programs aimed to boost housing, urban renewal, highways and other public works, and defense spending, we also have the very powerful influence of a tax cut to consider. There is obviously considerable difference of opinion about the need for a tax cut in Washington. I would venture the opinion that we had better have the tax cut, and quickly, with some relief to corporations as well as individuals, in order to stimulate new private investment as well as new purchases. The effect of a tax cut will not be as immediate as some people seem to think, and this is one time when it would be safer to lock the barn door *before* the horse is stolen.

Now comes the problem of trying to assess the balance between the forces of good and the forces of evil. There is no neatly calibrated scale on which we can weigh these things and come up with a precise mathematical balance. It has to be a matter of subjective judgment, and yours may well differ from mine.

In my opinion, the downward forces have not yet been routed. I think they can be defeated fairly easily, but it will take more recognition of the problem in high places than I have observed so far.

We have not yet reached the bottom of this business dip.

But it is not going to keep on going down and down. We don't have the makings of a real depression. This is not another 1929.

Why?

First, as I have said, we have a growth economy and a growth attitude. In 1929, we had the attitude (on a much more speculative basis, however) but the real growth of the economy was deceptively low, particularly from the population standpoint. Birth rates had been decreasing for years, small families were becoming popular, and we had virtually shut off immigration, which had earlier been a main source of growth. Currently, we have been, and still are, in a much more vital state.

Second, we have many cushions under the economy that we didn't have in the 1920's. Widespread unemployment compensation, universal use of amortized mortgages, deposit insurance, social security, better policing of stock market operations are just a few. And whether you like it or not, government activity is a much bigger share of the total economy than it was

in 1929—and government activity should not be subject to the same cyclical forces that affect business.

Finally, we are much more sophisticated about our economy than we were then. We still don't know very much about what makes it sick, and how to keep it well, but we do know vastly more than we did in 1929.

As to immediate prospects, we have several opinions to choose from. There is still the "second-half club" rapidly becoming the Fourth Quarter Club, which thinks things will start to boom later this year. There are others, very few in number, who think the slump will go on down and down into a depression. And there are some, including myself, who think that we will witness a bottoming out within a few months, followed by a relatively mild upturn for another period of months. We have become accustomed, in the post-war years, to finding businesses of all types setting new records with almost monotonous regularity. In writing press releases in our own office about construction contracts, we have exhausted the dictionaries trying to find new ways to say the same old thing month after month and year after year as construction contracts regularly hit new peaks.

I rather doubt that we will see new records set in general business activity for some time to come. The upturn from the recession will probably show up in a very few months, but I think it would be wise not to expect a runaway boom in business. It would be more prudent, I believe, to expect a period of good, but lower-than-record business activity.

Back in college, I had an economics professor who used to keep a large crystal ball on his desk, with a smaller crystal ball alongside of it. When anyone asked, as they usually did, why one crystal ball wasn't enough, he always replied, "The big one is for long-range forecasting; the little one is only short-range."

I've always remembered this not because it was particularly hilarious but because it did emphasize something we are all too prone to overlook. There are two futures, long-range and short-range. Most of our attention is devoted to the short-range. How will the summer's vacation business be; will Fall sales of clothing hold up; what's the outlook for housing in 1958; where is our next meal coming from?

I don't blame any businessman for putting first things first, but it is unfortunate, because we are prevented from seeing the forest of the future by looking at the trees of today. The short-term outlook is here today and gone tomorrow; the long-term, by definition, is much more important because it will be with us for years to come.

Recessions are always short-term. The longest of them lasts only a small fraction of a lifetime.

We stand at the threshold of not one, but three new eras, any one of which could revolutionize our lives. One is atomics. One is electronics. And the third is autologics, of machines that add thoughtpower to our already enormous horsepower. We are in the primitive stages of a more fantastic era of growth and change than even Jules Verne could have conceived.

Anyone who stands around too long musing about the outlook for 1958 is likely to find that history has left him far behind.

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Building and Real Estate Investment in the Sixties

It seems to be pretty well agreed that the decade of the Sixties is going to be a period of sharply accelerated activity in building and home financing. It's expected, but precisely what is the basis for these expectations? That is what Mr. Warnecke does here, analyze the various factors which represent the basis for these great expectations in the coming period. His conclusions are that what we are expecting will materialize all right but, he asks, "are we prepared for a new real estate boom of this magnitude?" We are, but three factors stand out importantly: thrift must be encouraged more, new investment sources must be tapped (the private investor must be lured back into the real estate field) and, finally, the threat of inflation must be met and beaten. Mr. Warnecke heads George W. Warnecke & Co., in New York.

By **GEORGE W. WARNECKE**

THIS is a period of retrenchment. Coupled with a general recession in business and industry, we have had fewer housing starts, slower home sales, more delinquencies, more vacancies—and some, let's face it, out-and-out failures of speculative real estate ventures.

Sometimes, as we watch the economic storm clouds drift by, we may begin to wonder how to reorient ourselves in these changing times. Are traditional policies still justified? Is real estate (absorbing more than $35 billion of life insurance funds alone) deserving of our continued confidence? Is it right to maintain and expand real estate loans as an outlet for investments?

G. W. Warnecke

At such times, it is appropriate to remind ourselves that the future of real estate is basically sound. Its broad outlines are *not* just visible through well-polished crystal balls. They are already well known from the facts and data collected over long periods by statisticians and economists.

All we need to do is to line up the various elements which make up the future of real estate in this country and a picture emerges which is indeed over-poweringly brilliant.

Population pressure: As Secretary of Commerce Sinclair Weeks pointed out recently, our population will increase by 28,000,000 within the next ten years. That means that every acre of land in this country will have to feed, house and generally serve eight people for every seven who live on it today.

Economic Growth: Within ten years, employment will rise by 14 million from 66 today, personal income will increase $100 billion and our gross national product will add nearly 50 per cent.

Number of Households: According to the Bureau of the Census, the number of households will increase from 49 million in 1957 to 60 million in 1970 and 64 million in 1975.

These are the basic economic facts. What do they portend for the categories of housing in which the institutional investor is likely to be interested?

Single Family Housing: Families—defined as a group of two or more persons living together and related by blood, marriage or adoption—should increase from nearly 43 million in 1956 to about 54½ million by 1975, a rise of 27 per cent, it is reported by the Metropolitan Life Insurance Company. The Bureau of the Census adds that the number of married couples will rise from 37.6 million in 1955 to around 50 million in 1975, a gain of 11 to 13 million in 1975. These families will be formed at a slightly earlier age (the median marriage age for women will be between 19.7 and 20.2) and will be somewhat larger than they are today. Architectural Forum estimates the number of average housing starts ten years from now at 1,500,000 as compared to the much-talked-about 1,000,000 today.

An increase of 50 per cent in the number of single family home starts seems somewhat more than the proportional increase in population and

the number of households. However, it is, perhaps, not over-optimistic when we consider the fact that many of the lesser developed areas of the country have never had a single family housing boom, that our builders and engineers will perfect further methods for mass fabrication of housing and that, after all, experience has shown that it is always possible to sell more homes, the only questions being "What kind of homes?" and "At what terms of financing?"

Multiple Family Apartments. Here is where I expect, and apparently Architectural Forum agrees, the greatest increase in both demand and supply will take place, that is a rise from 100,000 to 200,000 or 300,000 units annually. As more couples marry and more couples marry younger, the trend will be—as it always has been—for them to seek out an apartment at a rental which they can afford. They will have no large savings, of course, but by no means should be considered low-income tenants. Many of the luxuries of the Fifties—swimming pools, air-conditioning, garden-type environment, playgrounds, etc.—will be taken for granted—and paid for—by these young couples of the Sixties.

The tendency toward middle-and-high-income rentals should be further boosted by an increase in the number of older people, especially those over 65, which has been much talked about but still deserves all the critical attention it is getting. Our older population will add more than 5 million (an increase from 14.4 to 19.5 million) by 1970, it is reported by the Metropolitan Life Insurance Company.

We, who are familiar with the residential leasing and management business, know the retired or semi-retired person over 65 to be a first-class tenant of a well-run, well-serviced and high-to-middle-income apartment house development. Many of them had left the big cities to bring up their children in the country. But they are now returning to enjoy some of the sophistication and amenities and entertainment of big city life.

As the price of land will rise, taxes will be boosted and servicing costs mount, such larger units will be more economical to build and to maintain than the smaller, individual homes. The investor can get his share of the benefits of these developments by helping the right kind of conscientious multi-family unit builder get started today.

Industrial Construction. On this phase of the construction industry, Architectural Forum appears to be more bullish than industrialists themselves. It anticipates that the annual rate of factory building will be more than 70 per cent higher than now by 1967. McGraw-Hill's survey of Business' Plans for New Plants and Equipment indicates that businessmen expect to reduce capital expenditures in the late '50's and maintain a new level of $30 billion per year in the early Sixties, which would be $4 billion less than in 1958.

Actually, this appears to be one segment of the real estate picture in which forecasts pegged to particular years or periods are somewhat less than helpful. Experience has shown that industrial construction is closely connected with the current state of the economy. The investor can safely postpone a decision on such projects until the moment of actual submission.

On the whole, it does appear as though the industrial development boom is only coasting along. Undoubtedly, it will pick up again after 1960, and we can then decide on the basis of each particular project and the industry from which it is submitted whether it warrants a loan with an extended pay-out period.

Office Construction. Architectural Forum looks for a 28.8 per cent increase in warehouse, office and loft construction over the next ten year period. This estimate appears conservative and well supported by the current trend toward smaller follow-up booms in office construction in cities of a less than metropolitan character.

As more and more sub-metropoles are created and industrial belts connect more of the larger cities of the east, the need for more office space is likely to undergo a radical upswing. However, location factors in office construction will become more important than ever. The more secondary locations vie for investor consideration the more difficult it will be to weed out the office building with a real future from the speculative real estate promotion.

Schools, Hospitals, Churches and Highways will naturally continue to grow mushroom-like wherever new population centers are formed or interconnected. Architectural Forum estimates total outlays for public construction and for religious, educational, hospital and other nonresidential private construction at more than $23 billion by 1967.

Are we prepared for a new real estate boom of this magnitude? The answer has to be a very cautious "Yes, if . . ."

There are no projections available on the amount of investment capital available for real estate investment in the 1960's. We must therefore look to the record of the past years in order to assess the future.

In a recent study of the investment outlook, Bankers Trust Company says, "The prevalence of inflationary forces . . . apparently did not curtail the public's disposition to save. . . . However, much of the increase in saving . . . was used to repay consumer indebtedness; the flow of savings into the hands of institutional investors expanded only slightly. Savings were insufficient to meet current demands for investment funds. . . ."

During the years from 1954 to 1956, for instance, our gross national product rose steadily but the influx of investment funds into major savings institutions including life insurance companies, mutual savings banks, savings and loan associations, corporate pension funds, commercial banks and state and local government retirement funds actually fell off from $19.1 billion in 1954 to $17.9 in 1955 and $18.8 in 1956. As a result the increase in mortgage ownership went from $16.6 billion in 1955 to $14.6 billion in 1956 to $12.5 billion in 1957.

These facts point up the three major problems of capital accumulation in a rising economy:

1. **Thrift.** The last word on whether our financing institutions can meet the demands of an expanding economy is spoken by the consumer. It will be the task of life insurance companies, savings banks and other institutions to bring home to him the importance of saving not only by preaching moralisms and homilies

"An increase of 50 per cent in the number of single family home starts seems somewhat more than the proportional increase in population and the number of households. However, it is, perhaps, not over-optimistic when we consider the fact that many of the lesser developed areas of the country have never had a single family housing boom, that our builders and engineers will perfect further methods for mass fabrication of housing and that, after all, experience has shown that it is always possible to sell more homes, the only questions being 'What kind of homes?' and 'At what terms of financing?'"

but by offering the incentives and returns which provide the only tangible evidence of the worthwhileness of prudent habits.

2. **Tapping New Investment Sources.** But not only must we devote infinite care and patience to the development of the highest possible rewards to the prudent saver or life insurance buyer but we must also make sure that we offer the greatest variety of "products" to our enlarged market and that we do not leave any sources of new investment capital untapped. As a real estate man, I am particularly conscious of this need, for I feel that we have still not succeeded in opening up real estate as a form of investment to the general public—and thus maximizing the private investor's return. The entry of the private investor into the real estate field, if it can be achieved with safety or principal, should not be feared by the large financial institutions but rather become hoped-for and wished-for as a partial answer to our increasing requirements for new investment capital.

3. **Inflation.** Lastly, I feel that it will be difficult, if not impossible, to maintain a strengthened flow of investment capital unless every effort is made to curb inflation in both its primary effect as a deterrent to saving and its secondary effect as a premium paid to a spending-happy government which eats away both the investor's return and his capital.

If we cannot find a way to stop inflation permanently, it seems to me we should at least vary archaic rules on long-term mortgage security and permit the investor to add an inflation-equalizing equity interest (say 5 to 10 per cent of the total appraised value) to his security interest or defeasible title which would accrue as soon as the ten or fifteen year term of the mortgage has ended, and the mortgage has been paid off.

Such a clause, which would naturally require statutory authority, would give the investor a well-deserved share in the general rise in real estate values and protect him from the dilution of his invested principal.

In closing this discussion of the real estate outlook for the coming decade, I feel impelled to express my personal thankfulness for the opportunities before us to serve the investor and the public generally in realizing higher housing standards. I well recall a time when real estate came right after nitroglycerine driving as a dangerous form of business activity and when many small and one big depression all but demolished our faith in the future.

Today, we are getting set to reap the rewards of many years of hard work and—moderation—which have set the stage for undreamed-of wealth and prosperity.

» RENTAL HOUSING NEEDS: A 34-point program to help private enterprise meet the nation's rental housing needs has evolved from an extraordinary two-day conference in Pittsburgh. It calls for two changes in federal law but stresses: "What we need to make Washington's help effective is not so much new legislation as a new attitude, a new helpfulness and a new understanding" . . . in Congress and administrative agencies.

It calls primarily for more effective local action and leadership and more emphasis on cutting costs of land and construction.

The Pittsburgh session was co-sponsored by *House & Home* and the American Council to Improve Our Neighborhoods. Participants and observers were HHFA Administrator Albert M. Cole, Urban Renewal Commissioner Richard L. Steiner, Redevelopers William Zeckendorf and James H. Scheuer of New York, President Richard K. Mellon of T. Mellon & Sons, President Frank L. Magee of Alcoa, President Fred C. Foy of Koppers Co., President David G. Hill of Pittsburgh Plate Glass Co. and President Mark W. Cresap Jr. of Westinghouse Electric.

The Round Table made these two recommendations for changes in federal legislation:

» Let FHA offer new equity financing for commercial development as an inducement for low residential rents. "This is the only way low rent hous-

(Continued on page 33, column 1)

END FIXED RATES ON

THE Federal Reserve System carries out its trusteeship over the total supply of money and credit by regulating the availability and cost of commercial bank reserves. Through open market purchases and sales of Government securities, changes in rediscount rates and in reserve requirements, the System expands and contracts commercial bank reserves in accordance with its judgment of the credit needs of a fluctuating economy. These operations have the most direct effect, of course, on the flow of bank credit and money; but through ensuing changes in interest rates and yields, influence the flow of funds in all financial sectors. Thus, while so-called "non-monetary intermediaries," such as savings and loan associations, savings banks and life insurance companies, are not directly regulated by the Federal Reserve, their market operations are clearly affected by System actions.

Monetary policy is usually attuned closely to general business conditions. It is generally restrictive when inflationary pressures are threatening and expansive when deflationary forces are dominant. Monetary measures alone cannot control the forces of inflation and deflation. They do tend, however, under conditions of inflation, to make mortgage funds, as well as funds for corporate and state and local government investments, more limited and costly; and under deflationary conditions to make such funds more readily available at reduced interest rates and on more favorable terms to borrowers.

The actual allocation of the available supply of funds within the money and capital markets is a function of private competitive forces, and not of central monetary policy. It is not now the objective, nor is it within the power, of the Federal Reserve System to allocate credit to particular markets. Individual lenders and borrowers competing for loans and investments determine in the end the types of credit flows and their uses. Because of special institutional arrangements which characterize mortgage markets, however, the influence of monetary policy in this area is unique among capital markets.

Owing mainly to the fact that a large sector of the residential mortgage market is influenced by Federal statutory and administrative actions, lenders and borrowers have not been as free to compete as have participants in other sectors of the capital market. In particular, the policy of maintaining fixed interest rates on FHA-insured and VA-guaranteed loans has interfered with the allocative function of free market processes and has intensified the impact of monetary policy on the mortgage and real estate sector.

During periods of capital market stringency, such as 1951-1953 and 1956-1957, fixed interest rates on federally underwritten contracts, in the face of rising yields on other loans and securities, place mortgage borrowers at a distinct disadvantage in competing for limited investor funds. During periods of capital market ease, on the other hand, such as 1953-55 and 1958, when funds are ample and interest rates and yields on alternative investments are declining, FHA and VA mortgage loans again become attractive to investors.

Thus, alternate easing and tightening of monetary policy and capital market conditions during the postwar years, have been accompanied by exaggerated swings in federally underwritten mortgage flows. These shifts have coincided with the narrowing and increasing spread between fixed interest rates on federally underwritten contracts and flexible yields on corporate and other bonds. The flow of conventional mortgage funds, on the other hand, has fluctuated within a narrow range, as lenders, at least, have been free to adjust interest rates and other terms in accordance with changes in financial markets.

The question frequently arises of why, despite fixed maximum interest rates on FHA and VA loans, the technique of paying discounts or premiums has not been effective over the years in adjusting yields on these mortgages to actual market conditions? Other capital market securities, bearing fixed contract rates of interest, typically trade at prices above or below par with resulting yield flexibility. The answer lies only partly in the Federal restrictions placed on discounts on FHA and VA loans, ranging from those of uncertain legality in earlier postwar years to the rigid controls in effect for a time in 1957 and 1958. Part of the answer lies in the unwillingness of lenders to accept large discounts on FHA and VA loans, in the face of widespread opinion that such practices are somehow immoral or unsavory, notwithstanding the facts of market forces. The full answer lies in a myriad of factors beyond the scope of these observations, but clearly Federal restrictions and moral pressures on mortgage lenders severely limit the effectiveness of discounts in

FHA AND VA LOANS

and reduce the swings in the mortgage market says economist in analysis of monetary policy

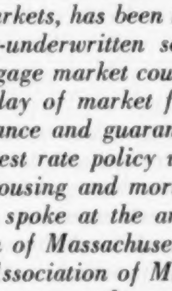
More and more the feeling grows that, come what may and whatever the obstacles—real and imagined—FHA and VA rates must be freed from their present straight-jacket control.

Mr. Klaman says that the policy of maintaining these fixed interest rates "has interfered with the allocative function of free market processes and has intensified the impact of monetary policy on the mortgage and real estate sector." In periods of tight money, such as in 1957, mortgage borrowers were at a distinct disadvantage in competing for limited investor funds, particularly those seeking federally-underwritten mortgages. The conventional market, free to adjust interest rates and other terms in accordance with changes in financial markets, has been much more stable than the federally-underwritten sector.

He suggests that the wide swings in the mortgage market could be reduced by permitting the "free interplay of market forces to set a price on Federal mortgage insurance and guarantee." Consideration now of a flexible interest rate policy which would contribute to high level stability in housing and mortgage markets is what is needed. Mr. Klaman spoke at the annual Trustees Day of the Savings Banks Association of Massachusetts in Boston. Prior to joining the National Association of Mutual Savings Banks he was for 12 years on the staff of the Federal Reserve System in Washington.

By **SAUL B. KLAMAN**

Economist, National Association of Mutual Savings Banks



achieving yield flexibility on FHA and VA mortgages.

The much greater stability of the market for conventional than for federally underwritten mortgages in recent years of change in monetary policy is evident from the record. From 1952 when money was tight, and 1955, when it was easy, the annual net flow of funds into conventional home mortgages increased from \$4.3 billion to \$5.7 billion, a rise of about one-third. The subsequent decline to \$5.3 billion in 1957 when capital markets were again tight, represented a drop of less than 9 percent.

During these same years, the net flow of VA mortgage funds was rising from a low of \$1.4 billion to a peak of \$5.3 billion, a nearly threefold increase, and then dropping again to \$2.3 billion, a decrease of well over one-half. Somewhere between these two extremes was the shifting flow of FHA mortgage funds.

Other basic forces are always at work modifying the influence of monetary policies in the mortgage and housing markets. One of the difficulties of living and working in the real world rather than in the world of textbook economics is that, in attempting to assess the influence of one set of forces "all other things cannot be held equal." In our dynamic economy "other things" are always changing. Thus, not only monetary policy, but changes in the closely related area of fiscal policy, in markets for corporate and other securities, in flows of savings to financial institutions, and in other market forces, have played a fundamental role in influencing the course of mortgage market developments. Moreover, Federal policy actions in the area of housing finance, seldom coordinated with those of monetary authorities, have tended on occasion to limit as well as to increase the effectiveness of monetary measures. Thus, the influence of changes in federal mortgage underwriting programs, in FNMA operations, in policies of the Federal Home Loan Bank System, must be carefully weighed in appraising the effectiveness of monetary policy.

While it is clearly hazardous to try to lend precision to the measure of

influence of monetary measures, there can be little doubt that the effective operation of a flexible monetary policy has been of fundamental import in mortgage market activities. This policy had its postwar birth with the Federal Reserve-Treasury "accord" in March 1951. Prior to that date financial institutions enjoyed nearly unlimited liquidity as a result of unusually large holdings of Treasury securities and Federal Reserve support of their prices. Monetary policy was largely inoperative as investors were able to liquidate Government bonds readily and without penalty to acquire higher yielding assets, and in particular, to build up depleted mortgage portfolios. Thus, all major types of savings institutions steadily increased their share of capital market investments going into mortgages in the five years ending in 1950. That the same uniformity of behavior has not prevailed since early 1951 must be attributed in important measure to the reactivation of a positive monetary policy.

The major types of lenders have reacted differently to monetary measures, reflecting other basic and changing conditions, in part peculiar to the type of financial institution. Moreover, we find the same types of institutions reacting differently to similar monetary actions taken on separate occasions. Thus, notwithstanding the general tightening of credit between 1951 and 1953, and the accompanying marked reduction in the total net flow of VA mortgage funds, the mutual savings banks expanded their net VA mortgage investments by two-fold. As a result, the participation of savings banks in VA mortgage markets increased from less than 10 per cent in 1951 to more than 50 per cent in 1953. This unusually large share has since been reduced, but savings banks have continued to be the largest VA mortgage investor through periods of both credit stringency and ease.

In contrast to the accelerated activity of savings banks in VA mortgage markets despite credit stringency, their investments in conventional home mortgages between 1951 and 1953 were being markedly reduced. During this same period, the total net flow of conventional home mortgage funds from all sources was nearly doubling.

Another way of saying these things is that during the 1951-53 period of credit tightening, savings banks were reacting in a completely opposite manner from life insurance companies and commercial banks. Both of these groups were curtailing their VA mortgage flows and expanding their conventional mortgage flows. Savings and loan associations were also increasing their conventional home mortgage lending in this period, but these institutions were expanding their VA loan activity as well.

Now, how did the main types of financial institutions react to monetary stringency in 1956-57? This time all investors, savings banks and savings and loan associations, as well as life insurance companies and commercial banks, sharply curtailed their VA mortgage activity. Conventional mortgage flows from these lenders declined by relatively small amounts.

During the intervening 1953-55 period of monetary and capital market ease, the greatest expansion in mortgage funds from all types of financial institutions occurred in the VA mortgage market. In periods of both ease and stringency, the timing and degree of change in mortgage flows varied considerably among investors. The response of life insurance companies, for example, was much stronger and involved a longer time lag behind changes in monetary policy than did responses of other types of financial institutions. This is a reflection both of the wider capital market investment opportunities available to life companies and the greater influence of the mortgage commitment process on their operations. In the savings banking industry, there is much less uniformity of operations, with some banks preferring to operate under a system of advance mortgage commitments, and others preferring to purchase on a spot basis in the open market.

What explanation can be offered for the uniqueness of the savings banks' action in aggressively seeking VA loans in the 1951-53 period of credit stringency, then reducing this type of activity by one-half in 1957 under similar credit conditions. The action of savings banks in Massachusetts in this respect was similar to that elsewhere, except that the 1951-53 expansion was much smaller, and the 1956-57 contraction was much greater relative to all savings banks. The answer to these actions lies in large part, I believe, in the considerably different legal and portfolio situation which existed for savings banks in the two periods.

In 1951, most savings banks had only recently acquired the right to lend beyond state boundaries, many of the larger banks had more funds available for investment than could be absorbed in local markets, and effective yields on VA loans after discounts in many out-of-state areas were favorable compared with local investments

available in the capital surplus areas of the East. By 1956-1957, on the other hand, credit stringency found many savings banks with mortgage portfolios at close-to-desired levels, discount regulations on federally underwritten loans increasingly restrictive, and the amount of discount required to compete with yields on other securities increasingly large, especially in view of unusually attractive corporate security yields.

In retrospect, I think we can agree that among the most significant developments influencing postwar mortgage operations of savings banks was the amending of state statutes to permit the acquisition of out-of-state federally underwritten mortgages. Prior to this legislation, savings banks had been reducing steadily their relative participation in mortgage markets. In the subsequent years, they have become important national mortgage lenders—gaining and holding leadership, in fact, in the VA mortgage market, as previously noted—in addition to their traditional and still significant role as local lenders.

Unless fundamental changes occur in the interest rate policy on federally aided mortgages, these investments may be expected to continue to be particularly vulnerable to changes in monetary policy and in the general financial climate. And because the savings banks have such a large proportion of their total mortgage portfolio in FHA and VA loans—three-fifths, as compared with two-fifths for life insurance companies, one-third for commercial banks, and little more than one-fifth for savings and loan associations — their overall mortgage operations may be particularly affected by changes in monetary policy as well as by unpredictable Federal statutory and administrative changes.

There are, of course, variations in portfolio composition among the savings bank states, let alone the individual savings banks. In Massachusetts, the percentage of federally underwritten loans is 45, somewhat lower than for all savings banks, and if Boston banks are eliminated, the percentage drops to about 40, still higher than the average for most other types of financial institutions. The safety added to savings bank mortgage portfolios by the high percentage of federally underwritten mortgage loans is, of course, comforting. It should be recognized, however, that to the extent that this portfolio composition reflects current lending policy of the industry as a whole, it will be more sensitive to changes in monetary actions than that of mortgage lenders more actively engaged in conventional loan markets. Savings banks continue to be limited in their conventional mortgage lending activities to the 17 states in which they are located or to adjacent states, while savings and loan associations are widely dispersed throughout the country, including the faster growing areas, and life insurance companies can generally make conventional loans anywhere in the United States.

For the future, potential changes in conventional loan arrangements may have an important influence on mortgage markets. Loan-to-value ratios of 90 per cent and extended maturities are already in effect in New York State for savings institutions under certain conditions. Some form of mortgage insurance for conventional loans with flexible interest rates, probably under Federal sponsorship, may not be far off. The efforts of savings and loan associations in this direction have been receiving consideration in Washington. All of this may mean important shifts in the structure of mortgage markets and in lender portfolio composition, with resulting changes in responses to monetary policy actions.

Meanwhile, overall 1958 mortgage market developments have followed a traditional pattern in a setting of monetary ease, reenforced by emergency housing legislation. As the business recession deepened, the Federal Reserve reversed its earlier policy and moved vigorously, beginning in November 1957, to establish a credit environment conducive to business recovery. It has acted on four occasions to reduce the rediscount rate and lower bank reserve requirements, and through its open market operations has expanded the base of commercial bank credit generally. There has been a resulting precipitous drop in short term yields which has carried over into the long end of the market, as investors receiving a greater inflow of savings than anticipated, have been actively competing for a limited supply of corporate bonds and mortgages.

In this setting, federally underwritten mortgages have once again become attractive investments, the more so in view of the recent elimination of Federal controls on the amount of permitted discounts and the statutory increase to 4¾ per cent in the contract rate of interest on VA mortgages. Some life insurance companies, however, have not yet been attracted to the VA market, because of previously built-up portfolios, and because discounts necessary to bring yields into competitive range are larger than they feel can be justified from a public relations viewpoint. Discounts required to bring yields on FHA mortgages into competitive range with other investments have declined throughout the country, and in some areas have disappeared. In Boston, the Boston Five Cents Savings Bank has ignored traditional market practice and is making FHA loans to borrowers at half a percentage point below the current administrative rate of 5¼ per cent, rather than go to premiums. VA-guaranteed loans in this city are now being made at par or one point above par. The metropolitan Boston area is, of course, unique in its mortgage practices, as well as in other respects, and the current market situation here is hardly representative of other parts of the country, nor even in other parts of Massachusetts.

Nonetheless, it is clear that there has been a turnaround in mortgage markets lagging customarily by several months behind the shift to monetary ease. Commitments from life insurance companies and savings banks have risen rapidly from low 1957 levels. Pension funds are becoming actively interested in FHA and VA loans after years of indifferences. Purchases of completed mortgages, especially from FNMA's portfolio, have increased considerably. Moreover, competition for mortgages may increase if the inflow of savings continues large, and the volume of new corporate security issues declines as is widely expected. Thus, contract interest rates on conventional mortgages are likely to decline further and prices for federally aided loans may rise somewhat. In this kind of competitive situation, it is especially important that savings bankers and other investors guard against a possible deterioration in loan quality.

All in all, unless residential construction and purchases fail to live up

(Continued on page 29, column 2)

Voice of the Home Office

"Let's Look at the Record"

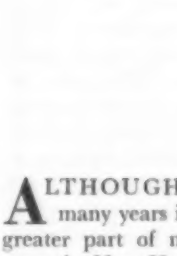
By **MARTIN C. BROOKS**

Director, Mortgage Loan Branch

State Mutual Life Assurance Company of America

ALTHOUGH I have lived for many years in New England, the greater part of my early years were spent in New York City. Not everyone in New York agreed with Governor Al Smith in those days, but everyone respected him. His favorite expression, spoken from the corner of his mouth in his own inimitable style, was—"Let's look at the record," —and that phrase has remained with me ever since.

When MBA President John C. Hall called me from Birmingham and asked me to write about State Mutual's investor-correspondent relationship, I was reminded of Al Smith's words. I believe a "look at the record" would tell the story better than any flowery narrative.



Martin C. Brooks

Thirty years ago State Mutual had 21 correspondents, and a grand total of $50,000,000 in mortgage loans. During 1928 we made what was then a remarkably big loan in Cleveland. It was for $350,000. Incidentally, that loan remained on the books until about a year ago. Of our 21 correspondents, one was a title company, ten were banks, and ten were firms that would be called mortgage bankers today.

Let's see what has happened since Al Smith's time. Of the ten banks that represented us then, only one does so today. But of the ten mortgage bankers, six are still servicing loans for us and, in one company we are now doing business with the third generation. Tradition enters our relatively short history!

At the recent dedication of our new home office in Worcester a correspondent was present who had attended similar ceremonies at the time we completed the annex to our old building in 1929.

When you consider that the past 30 years have included a major depression, a World War, and several other disturbing eruptions, this is a remarkable record of lasting relationships.

Now let's consider the part the mortgage loan organization has played in the post-war investment picture of State Mutual.

At the end of World War II we were firmly convinced that the interest rate structure was artificially low. We expected a readjustment. Fifty-seven per cent of our assets were investments with a maturity in excess of 20 years, and our mortgage investments stood at $70,000,000—representing only 24 per cent of the Company's assets.

We realized that if our premise were correct we would have to transfer a major part of our long term investments into short term holdings. Mortgages were ideal media to meet this problem, as they are for us essentially a short term investment. Other available forms of short term investments were equipment trusts and loans to smaller industrial concerns. However, mortgages generally offered better interest rates for our Company.

How our correspondent organization responded to this need is amply demonstrated by the fact that when the readjustment occurred and interest rates returned to a more normal level, we had only 20 per cent of our assets remaining in long dated investments. State Mutual's mortgage portfolio had grown to $271,000,000—45 per cent of its assets!

During this period mistakes were made, two of which were the way premiums and discounts were handled. Due to inflexible mortgage rates, we sometimes paid premiums for loans which the correspondent in turn paid to builders to get the loans. That was not good business. Subsequently, we had quite a period when inflexible mortgage rates created deep discounts. This also was not good, and I am glad to say that many life insurance companies were reluctant to purchase loans at these deep discounts.

Today the State Mutual correspondent organization has more than doubled in number since 1928. During this expansion we had a choice of two courses to follow: establishing branch offices or the correspondent system and we chose to go along the road with the mortgage correspondent. We are convinced that a properly set up mortgage correspondent is

the best organization for us through which to conduct a nation-wide mortgage business. We believe it has for us distinct advantages in the origination of loans, servicing of loans and economy of operation. We have not forgotten the contribution made by our correspondents to our post-war investment effort. We have taken a look at the record and found it good.

The flexibility which we believe is inherent in the correspondent system must not be lost if the system is to continue. It must, as against any other type of organization, be able to produce better loans, service loans better, be competitive as to costs, and alert to changing conditions. We do not know what the future holds in store for us, but we do know that we can and will work together effectively.

We are very proud of the men and the companies who handle our mortgage loans. We want them to succeed for their success is our success. We want them to be outstanding in their community, for they are our representatives. Our name is better known in their community because of their efforts.

We are also very proud of our Company's reputation and its 114-year "heritage of integrity." Our correspondents are an integral part of that reputation.

END FIXED RATES

(Continued from page 27)

to present prospects and the supply of mortgages becomes more limited, the flow of mortgage funds from all major types of financial institutions may be expected to rise appreciably this year over last. Partly because of lags in actual mortgage flows behind commitments and housing starts, I would expect mortgage lending to be even larger in 1959 than in 1958.

If this pattern is, indeed, realized then we will once again be on the upswing of the roller coaster path typically traced by FHA and VA mortgage flows. This path is hardly the road to high level stability in housing and mortgage markets. For as soon as business conditions change—as they surely will—and borrower demands increase, credit becomes less readily available, and monetary policy is directed against inflationary pressures, then the impact on the federally underwritten mortgage sector will again be substantially greater than on other sectors of the capital market. A basic step towards reducing swings in this important area of the capital market, and of the economy as a whole, would be to permit the free interplay of market forces to set a price on Federal mortgage insurance and guarantee. To be su*r*e, this step seems less urgent now that competitive yields have been reduced to the point where FHA and VA mortgages are once again attractive.

American families now own an estimated 270,000,000 life insurance policies—an average of five per family. This represents an increase of about 50,000,000 in the past five years.

• • •

Insured pension plans now number 23,640, a rise of 70 per cent from the 13,990 of five years ago. Today's plans cover 4,860,000 persons.

• • •

If the present highway toll continues, life insurance companies will pay out death benefits of $120,000,000 in 1958 for motor vehicle fatalities. This would be some $45,000,000 more than five years ago.

WE'RE GETTING LETTERS AND LETTERS . . .

. . . about this year's big MBA Convention at the Conrad Hilton Hotel in Chicago November 3 to 6. Most of them contain advance registrations ($25 for members and $15 for wives) and others are confirmations of hotel reservations. Have you made your plans, got your hotel reservation, registered in advance? If not, get them in the mail now before the summer interlude begins. MBA's 45th annual Convention will top them all. You can't afford to miss it.

President's Page

ACCOMPLISHMENTS OF A HIGH ORDER

WITHIN the next several weeks the so-called "regular" housing bill will be discussed, debated, changed and revised and out of the process will come something which will go on the books as the housing legislation of 1958. The Senate Banking and Currency Committee has just acted, as these observations are being noted, and what has been reported out represents still another step in the socialization of housing. That is a story to be told later as developments occur. What is particularly interesting to the mortgage industry at this moment is that the Senate bill will not include the proposal which, in the opinion of most people, would have greatly changed the character of the business as we know it. This was the proposal to insure 90 per cent of the top 20 per cent of loans amounting to not more than 90 per cent of value—that is, provided they were made by members of the Federal Home Loan Bank System and only these lenders. A new corporation was to be set up for this new type of lending and, as was generally agreed, lenders other than savings and loans would have been adversely affected had it become law.


John C. Hall

While it was reported favorably by the Senate Banking and Currency housing sub-committee, the full Banking committee rejected it. It appears dead for this session but there is just a chance that the House Banking and Currency Committee may pick it up. In any event, our MBA *Legislative Committee,* headed by Robert Tharpe of Atlanta, aided by many members throughout the Association, did a magnificent job in explaining and interpreting the significance of this unwise proposal and what might be expected of it. Their work, in the hearings and elsewhere, was an excellent example of a Committee at Work—hard at work, doing a conscientious job in meeting a challenging situation.

In the past few months I have used this page to recite some of the accomplishments of the various MBA committees this year and what the Legislative Committee recently did seems to be a particularly outstanding example of high performance. Our *Research Committee,* headed this year by Samuel C. Ennis of Hammond, Ind., is another group that deserves high commendation. This year it set out to make a broad investigation of areas in which scientific research is needed to benefit the mortgage industry. Almost fifty proposals were examined, practically all of which merited careful consideration. Five have been singled out for research projects: 1. The single audit; 2. Single interest hazard insurance for mortgage investors; 3. The question of management succession; 4. Compilation of a glossary of terms and phrases used in mortgage lending and investing; 5. A study of branch office operation. Each one of these is a challenge—they all represent things that would either be beneficial to have or areas of our business where the facts are few or little known.

Another vitally important MBA group is our *Insurance Committee,* headed this year by Howard E. Green of Chicago. It is an alert, conscientious group with an important assignment but not all of the excellent work which it does is fully appreciated. And, too, many of the problems which confront it can only be solved at the state level where our advice and counsel are sought but where, in the end, it is the members in that particular state who do the work. The Insurance Committee deserves our thanks. And, to repeat, so do all the other Committees which have worked so well this year. As MBA grows, more and more work must, of necessity, be done in committee. It's the history of all organizations. It is working well within MBA.

John C. Hall

PRESIDENT

Servicing Tips from the Top

A monthly department about Mortgage Loan Servicing conducted by W. W. Dwire, Vice President, Citizens Mortgage Corp., Detroit, and member, Mortgage Servicing Committee

How to Reduce Your Volume of Late Notices with Good Results

By **RAYMOND L. DAVIS, JR.**
Treasurer, Murphree Mortgage Co., Nashville

LIKE most companies, our firm sends two late notices—one on the tenth of the month and one on the fifteenth. A recent analysis disclosed that the first notices were going to approximately 20 per cent of our total mortgagors. It was further discovered that 15 per cent of these mortgagors always made their payments so as to reach our office no later than the twelfth of each month indicating that these people apparently made their mortgage checks out on or about the tenth of the month, at the same time they paid their other bills. Their payments and our late notices crossed in the mails.

The records pertaining to this group were pulled and marked excellent. A letter was then sent to each of these mortgagors explaining that our records disclosed they had never failed to make a payment after the twelfth day of the month, that we had marked our records "excellent" and effective immediately were discontinuing sending to them the tenth of the month notice.

Their response to this action was overwhelming. We received numerous phone calls and letters from these people stating that they appreciated our discontinuance of the sending of this notice and that, in return for our recognition, every effort would be made on their part to live up to our excellent rating. As a further result of their appreciation, we have obtained new business that we feel sure would not have been obtained otherwise. Furthermore, our mailing costs have been reduced as has the burden of sending notices. Also, since the initiation of this procedure, not one among this group of mortgagors has been late because of a failure to receive a notice.

Reduce Your Year End Mailings with a Savings in Cost to You

By **JAMES I. McFAUL**
Controller, McMillan Mortgage Company, Los Angeles

IF YOU are using punch card payment coupon books, here is an idea that will save you money and, at the same time, provide a certain convenience to your mortgagors.

Include with your book of payment coupons a statement of the results of the escrow audit in those cases where a shortage exists. This statement will represent an invoice for the amount of the deficit. Also include the year end statement containing the information provided your mortgagors for tax purposes and other information. As a further convenience to your mortgagors, one of the inside covers of the coupon book can be printed in ledger form to provide a convenient means for maintaining a record of their payments.

Direct Payments to Custodial Bank

By **A. A. JOHNSON**
Vice President, Colonial Mortgage Service Company, Upper Darby, Pa.

A PLAN to accelerate the depositing of mail receipts of monthly payments and to eliminate certain details, was inaugurated at Colonial Mortgage Service Company two years ago which has proved to be successful. Colonial was among the first to adapt into mortgage servicing an established practice followed by some manufacturers and insurance companies.

The plan calls for payees to address the servicer through the use of a post office box number. The contents of the box are delivered directly to servicer's bank which in turn endorses and deposits all receipts and transmits accompanying coupons to the servicer for the processing of payments received.

Through the system, the volume of incoming mail at the servicer's office has been greatly reduced and the funds deposited at an earlier date. It has eliminated the endorsement of many checks and the preparation of deposit tickets. Besides reducing certain costs, the servicer has tighter controls on monthly payments received.

This is a new department of THE MORTGAGE BANKER *planned for regular monthly publication. As its title indicates, it is aimed at passing along cost-saving suggestions in servicing. The contributions will describe the idea but if more detailed information is desired it can be secured by writing to James G. Wasson, Director of Servicing and Accounting, Mortgage Bankers Association of America, 111 West Washington St., Chicago 2. And if you have some suggestions for publication here, Mr. Dwire will welcome them.*

You Can Use Your Clearing Account for Making Disbursements

By R. B. DENEWETH
Assistant Secretary, Citizens Mortgage Corporation, Detroit

MOST mortgage companies are using a clearing account for the daily deposit of total mortgage payments and then have their custodian bank simultaneously transfer these total deposits to the various custodial accounts by a transfer summary authorization or other acceptable authority.

This same procedure working in reverse will save substantially on the number of checks written during the period of a year. Instead of drawing separate checks to each payee covering disbursements from each custodial account, prepare one check on your clearing account to each payee for the total of all items and then by summary authorization instruct your custodian bank to charge the various custodial accounts in the appropriate amounts and credit the total proceeds to your clearing account against which the disbursement is made.

RENTAL HOUSING NEEDS

(Continued from page 23)

ing can be subsidized at no cost to the taxpayers," says the Round Table. "It subsidizes low rents for housing, not out of taxes, but out of by-product commercial profits and land value appreciation. If a new rental housing area is so planned that the residential developers can be reasonably sure of retaining by-product commercial profits, they could often make so much money on the commercial that they could well afford to break-even on the residential (just as many builders sell their houses close to cost in order to cash in on the by-product commercial increment). Such a tie-in is already authorized by both Sec. 207 and Secs. 220 and 221 (which cover FHA rental and urban renewal units), but a housing act amendment is probably needed to make this provision broad enough to support minimum residential rents out of the commercial and industrial land value increment that big housing development or redevelopment generates."

» Give real estate investment trusts the same conduit treatment which now exempts all other security investment trusts from federal corporation taxes. This would help attack risk capital which is needed in "abundance" if the nation is to get "any large volume of good moderate rental housing. Without this conduit treatment the real estate trust must earn more than 16 per cent if it is to yield 8 per cent to its beneficiaries"—a fact which channels risk capital heavily into construction of luxury rent units.

Financing is the overriding problem of rental housing, the conference concluded, and financing moderate rental projects means mortgages backed by FHA insurance because "without FHA insurance, state laws make it illegal to finance rental construction with big mortgages (at least 90 per cent of value) and small equities (not over 10 per cent). Without big mortgages the high cost of equity money (15 per cent or more today) would price rental housing out of too much of the market."

The Round Table recommended these other ways the federal government could help:

» FHA should change its attitude toward rental construction. Rental housing could be made to work if FHA "would promote its rental housing programs, streamline its procedures and accept the risks it is paid to accept. Instead of assuming risks and spreading them, it has often been so cautious and given such low appraisals that many builders have found they could get bigger mortgages if they steered clear of FHA."

» Congress should take a new attitude towards FHA. "FHA is understaffed and underpaid. Congress will not let FHA spend enough of its own business income to do its job right. And Congress will not let FHA raise its salary scale high to hold or attract the high grade appraisal talent FHA needs." Ever since the windfall scandals of 1954, FHA's rental housing operations have been "demoralized." The reason is that "the purge taught FHA directors the hard way that it is safer to say no and taught FHA appraisers the hard way that it is safer to underappraise. . . . Neither the Republican Administration nor the Democratic Congress seems willing to recognize FHA as a self-supporting operation, well paid to spread and insure reasonable risks and so make loans safe collectively that might involve too great an exposure singly."

» Washington needs to take a new attitude toward small equity mortgage loans. "The nearer we can safely get to 100 per cent mortgages, the more rental housing will be built, the less high yield equity money will be needed and the lower rents can be profitably set. No matter how high the loan-to-value ratio allowed, today's builder has no chance of a windfall profit, for the cost certification required since the 608 probe makes mortgaging out impossible."

» There must be a new attitude toward the builder. Builders cannot be expected to wait ten years for their profit. "To stay in business and continue building, the builder needs to get his money out of each project fast. Until he does, he cannot use his capital to start another job. There is no good reason why a builder should wait for his profit on a rental housing project any longer than he waits for his profit on a for-sale housing project," says the Round Table.

» A new attitude is needed toward trading-up. "We could meet America's rental housing needs a lot faster and better if Congress would accept the simple and obvious truth that low income families can seldom afford new homes any more than they can afford new cars; that an active market for used homes is as important to the new house market as an active used car market is to the new car market; and low income families can get a lot more for their money in a used home than in a stripped-down new one which has most of the new house advantages stripped out to get the price down.

"In a million-house year only two U. S. families in 100 can expect to move into a new home. Why is there so much agitation, in Congress and

(Continued on page 34)

RENTAL HOUSING NEEDS

(Continued from page 33)

out, to build these two new units for people who cannot afford them instead of for people who can?"

» FHA should rewrite its property standards on rental housing. They should provide much more storage, much more thermal insulation, more adequate wiring, better noise insulation and more sound privacy. FHA should raise room size standards to at least equal public housing minimums and should encourage some provision for private indoor-outdoor living.

"Don't expect Washington to do the whole job," warns the Round Table, as it lists these other steps which should be taken locally:

1. Don't look for any quick and easy answer. "There is no panacea."

2. Find out first how much new rental housing is needed, how much old can be salvaged.

3. Try to cut land and construction costs by at least 20 per cent to make the rents lower. This will require "bold action to control land costs."

"Unless you hold your land costs down there is not much use cutting the costs of construction, for most of these construction cost cuts would not be translated into lower rents; they would just be capitalized in higher land prices."

4. Realize new rental housing alone will not cure slums. Over-crowding, segregation, disease and bad neighborhood layout must be tackled simultaneously. "You cannot cure slums without doing something about ignorance and slum mentality. You cannot cure slums without raising the low living standards with which too many slum dwellers, for lack of education, seem satisfied. Unless you solve these social problems, all the money you spend to re-house slum dwellers in new rental units will just replace old slums with new.

5. New construction alone will not solve the rental housing problem.

6. Much can be done to ease the problem through rehabilitation of rundown rental units. "There is too much loose talk about building good homes new for low income families. With today's wages, today's land prices, today's materials, today's techniques, and today's codes, it can't be done without big subsidies—any more than the auto industry can build new cars cheap enough to fit the purses of the lower income market."

7. A lot more rental housing will be built faster if it is made profitable for a lot of small operators to build a lot of small projects rather than putting all the emphasis on big projects.

8. Avoid shooting for "impossibly low rents" in new units. Most renters can afford to pay quite a bit more rent if better housing were available for them and if they wanted a better home as much as they want other things.

9. No cost-cutting program should be pushed so far that it cuts the quality of a project. A cheap unit may help one poor family move out of a slum where a moderate rental unit may enable a half a dozen families each to make a jump to a better home—as in a game of musical chairs.

10. The demand for rental housing will be changing in the next 20 years and this must be taken into account in today's planning. The need of family-size units for white families is decreasing while it is increasing for Negro families. In the next 20 years there will be more housing demand from single persons, aged and young couples.

11. "The first aim of rental housing should be to re-create a housing climate where the profit motive can work" and it works poorly "when bad housing pays so much better than good."

12. Every city's "first need" is a good city plan and a good regional plan—plus the courage and determination to carry it out. Only then can a city be made more livable and more families persuaded to stay in the city as renters.

13. Local businesses and businessmen should provide some of the equity money for rental housing. They will be paid off in two ways: once in direct dollars and again in community growth and prosperity.

14. A workable policy for minority housing must be found before there will be any sound and lasting solution to a rental housing problem. And this involves finding some way to make better homes available to Negroes with a high standard of income and education.

15. The actual need for rental housing can be cut and should be cut through more cooperative and low-equity ownership. Four reasons: a) nearly four out of five U. S. families prefer to own a home rather than rent; b) renting costs more than owning; c) ownership solves the equity money problem and d) federal housing policy makes owning a home as easy as renting.

16. Tax assessors should be persuaded not to overassess rental property.

Biggest Year Yet For Life Companies

The gain in total life insurance owned by American families with the American and Canadian life insurance companies in the first half of the year will probably be the largest on record for any comparable period, the Institute of Life Insurance reports. It is estimated that the total in force was in excess of $480,000,000,000 on June 30.

Such an attainment would carry life insurance ownership per family through the life insurance companies to more than $9,000—three times that of only 15 years ago. Eliminating those not owning any life insurance, the average per insured family would probably be in excess of $11,000. And this is on the basis of a record number of policyholders.

Purchases of new life insurance also appear to be setting a new peak in the first half of 1958. Preliminary indications are that they will be in the neighborhood of $33,000,000,000, in the first six months.

Contributing to the larger volume this year is the greater average size of ordinary insurance policy bought. Policies of this type, which account for two-thirds of aggregate life insurance currently bought, this year are averaging over $5,500. This is one-tenth larger than the average a year ago and almost one-third larger than the average two years ago.

Payments to American policyholders and beneficiaries will also reach a new peak this year. In the first six months, these payments will reach nearly $3,700,000,000, up about $400,000,000 over a year ago. Death benefits alone are estimated at over $1,500,-

(Continued page 40, column 2)

Stability on the Farm

Just as the agricultural sector of the U. S. economy has shown more stability than the industrial area during the recession and the immediate period before it began, farm lending too has not been subject to quite the same drastic changes which have affected urban lending. Farm loans, it is true, declined substantially last year but this field of credit reflected a certain stability not seen elsewhere.

THE $2,254 million in farm mortgages recorded in 1957 was about 6 per cent less than that for each of the two previous years. Aside from these two years, it was the largest amount in any year since 1923. The number of farm mortgages recorded was down about 5 per cent from the previous year. It was less than in any year since 1944.

These figures are based on estimates of farm mortgage recordings, including purchase money mortgages, for all lender groups except the Federal land banks for which loans closed as officially reported, excluding purchase money mortgages, are used. The estimates are made currently by the Federal land banks from reports of farm mortgages recorded in a substantial number of counties in each Farm Credit district.

Both the amount and number of farm mortgages of Federal land banks, banks, and insurance companies declined in 1957. The amount of loans made by the Federal land banks declined 23 per cent and the number 24 per cent. Estimated recordings for insurance companies were down 21 per cent in amount and 25 per cent in number and banks had 5 per cent less in amount and 3 per cent less in number of recordings.

The number of farm mortgages recorded by individuals was about the same as in the previous year but the amount increased 8 per cent. The amount for miscellaneous lenders increased 22 per cent and the number 23 per cent.

The average size of loan for all lenders was about the same as in the previous year. Percentagewise, individuals, with loans averaging 8 per cent larger than in 1956 showed the biggest increase. The size of insurance company loans increased 7 per cent and land bank loans 3 per cent. The average size of bank loans as well as loans of miscellaneous lenders declined.

The Federal land banks accounted for nearly 18 per cent of the total amount recorded. This was slightly less than in the two previous years but was larger than in any other year since 1936. Insurance companies accounted for 17 per cent of the total, the lowest since 1947. The 22 per cent of the amount recorded by banks was about the same as in 1956 and compares with 24 per cent in 1955 and a high of 35 per cent in 1946. Individuals and miscellaneous lenders accounted for a larger share of the recordings than in 1956.

The Federal land banks in three Farm Credit districts—Omaha, Houston, and Spokane — accounted for about 25 per cent of the amount of farm mortgages recorded by all lenders in 1957 in these districts. The percentage for the land banks ranged from nine per cent in Baltimore to 26 per cent in Omaha. It was less than in 1956 in all Farm Credit districts except Columbia where it remained about the same.

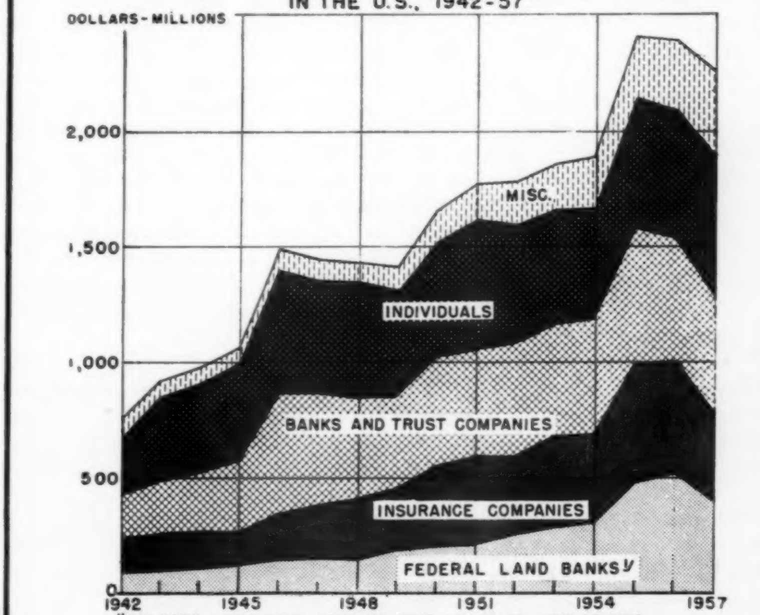
The per cent of the amount recorded by insurance companies was down in 10 Farm Credit districts. It was slightly larger for the Wichita district than in the previous year. It remained the same in Houston.

Banks had a larger percentage of total recordings than for the previous year in five Farm Credit districts—Omaha, Baltimore, New Orleans, St. Louis, and St. Paul—and in three districts—Louisville, Wichita, and Berkeley—the percentage was the same as in 1956.

Individuals increased their proportion of recordings in all districts except three. Of the total volume of mortgages recorded they accounted for 27 per cent compared with 23 per cent in 1956.

The estimated farm mortgage debt on January 1, 1958, for the United States was about 6 per cent more than at the beginning of 1957.

ESTIMATED AMOUNT OF FARM MORTGAGES RECORDED IN THE U.S., 1942-57



1/ INCLUDES LAND BANK COMMISSIONER LOANS TO JUNE 30, 1955

Operating Branch Offices

BRANCH offices are relatively new to mortgage banking. Many firms have had one or more branches for more than twenty years but the percentage of firms having any, even now, is very small. Mortgage banking is a form of service not fully subject to technological improvements. However, businesses such as manufacturing or fabricating have been able to take advantage of such improvements, thereby progressing very rapidly in their field the past quarter century.

However, there has been more progress made in mortgage banking operations in the past eight years than in all the prior years. To take full advantage of the technological improvements it has become necessary to add volume. Many areas in the United States have become static in population—some are even retrogressing with the availability of new mortgages dwindling.

When expansion of volume could not be achieved in the existing old trade areas, branches were opened. Another reason for opening branch offices was the insistence of a mortgagee's major builder moving into an area which could not be properly served from the home office. Some builders have had projects totaling thousands of units which gave a satisfactory basis of income with which to begin operation of a branch office. Still another reason has been at the request of investors, with whom the mortgage banker has an existing contract, to cover additional territory not within the practical servicing area of the home office. This type of request may be initiated from the desire of an investor to buy mortgages where investment funds are originated, such as life insurance premiums, for diversification or for any other reason that may motivate the investor through its investment officer, committee or board.

An example of this is the relatively new VHMC Program. The U. S. government and private investors have cooperated to take mortgage funds to remote areas to help eliminate the need of direct government loans. Mortgage correspondents with branches were better staffed and equipped to perform this service, and some others were induced to open branches, thereby gaining allotments of funds possibly not otherwise available.

The chief purpose of branch offices is to make services available in a local area. This will enable you to render faster, more efficient service by being on the spot to do so. Being more accessible, it is possible to render more service at less cost to the customer and to your company.

The branch office is a center for servicing personnel for origination of loans, collection of payments and administering to all other needs of the customer on the spot. The size of the organization should be determined by the amount of volume and types of business available. In the beginning, perhaps one man will be the forerunner of a sub-office and a sub-office the forerunner of a full branch. As the requirements of the customers enlarge, the types of services may be increased also.

It is advisable to localize your organization. Do your best to avoid an anti-chain store attitude. An example of the practice of the foregoing is the custom of lawyers to associate themselves with a local attorney if the matter necessitates a hearing in the courts. Care must be taken to avoid a hostile attitude and every practical method should be employed to forestall this. There should be participation in local activities, first, in your own field such as Real Estate Boards, Builders Associations, Appraisal Chapters and, in general fields such as Chamber of Commerce (Junior and Senior) and as many other civic and charitable activities as possible and practical.

This does not mean that you must employ a local man as manager. The first and most important consideration must be that the manager be qualified. A capable man will succeed whereas an unqualified "native son" can be a dismal failure in the operation of the office. It is far better to choose the qualified person from another town as manager and have him enter into the local affairs of the community. A qualified person who is able to properly serve the branch area, will overcome the prejudice and narrowness of a "native son" requirement. This should not eliminate a "native son" should he be qualified; in fact, this would be an advantage.

In placing personnel in management or supervisory positions in a branch, it is expedient to train them first for a period of time in another branch, if available, and also in the home office. This will even enable a person experienced in mortgage lending to become familiar with your individual company's policies, procedures, forms and methods—thereby saving embarrassment to the individual before the lower echelon of the firm who have more detailed experience but less capacity to manage.

Should none of the opportunities for expansion come your way, perhaps it will be necessary to seek a proper branch location. Contact the District Federal Reserve Bank or Branch closest to the considered area to determine what locations are rated the most logical economically. Should there be more than one location geo-

es of a Mortgage Company

What are the inducements for opening branches, how do you go about it, what operations are delegated to the branches and which ones remain in the home office—in short, what are the economics of branches for mortgage companies? Mr. Rainford who operates eight analyzes this aspect of the business, a relatively new development in the mortgage industry. He is a graduate of Northwestern University School of Commerce in accounting and finance. He was first employed by a certified public accountant and then joined the auditing staff of a national food chain. Later he entered the retail lumber business and ultimately activated a dormant mortgage company to promote the sale of lumber with FHA loans. Soon the lumber business was sold and full time has been spent in operating a mortgage business for 22 years. His eight branch offices are in three states.

By W. C. RAINFORD

President, Mercantile Mortgage Company, Granite City, Ill.

graphically logical, determine the most desirable from a mortgage standpoint. In other words, pick the one having the greatest need for mortgages and, particularly, your services. This does not necessarily mean a location where there is no competition.

Geography is important and it is recommended that additions to your present territory be contiguous if possible. FHA has territorial rulings that complicate violations of this principle.

After you have narrowed the field, the Chamber of Commerce statistics may be studied to help determine the most likely spot or location to succeed. Interpretation of the figures and statistics presented must be comprehensive enough to determine past performances in all stages of the economic cycle plus the all important future.

The adage relative to the better-built mouse trap causing a path to be beaten to your door is today an unquestionable exaggeration. Nevertheless, the physical location of your office need not be in the 100 per cent building or block in the town if you have chosen your proposed operating area with care. Available parking is an important consideration for customers and employees.

Selection of the location of a branch to be established from "scratch" will probably be best determined by first placing a field man or two to serve the business as it develops.

Mistakes could be made and it is well to be careful in assumption of liabilities from advertising to office space. Limit all contracts to a predetermined trial period so that fixed expenses will not exist after you have discontinued at a certain location.

Division of labor must be fundamentally thought of as to whether work should be performed at the home or the branch office. The factor weighted the heaviest in the decision should be "where can it be performed with the least expense and still be effective." There will be variations in the answer to this, influenced most by the degree of specialization achieved by the home office.

The following functions should not be interpreted to be a dogmatic edict. There are more functions than those listed, perhaps some even more important than the ones listed. The presentation is for the purpose of forming a pattern for an approach or for thought as to the division of functions and to illustrate the logic employed therein.

It is recommended that these functions be performed at the branch:

1. Taking of applications for loans.
   a. Personal contact with the borrowers.
   b. Obtaining the credit report and the interpretation of the information furnished by the local rating agency, completing the branch recommendation and supporting the opinion with more complete details by direct investigation, if necessary.
   c. Closing loans.
   d. Furnishing to the customer, upon request, normal or usual servicing information such as payment analysis, i.e., principal and interest break down, tax or insurance information, all of which have been accounted for by the home office.
2. Contacting sources of business.
   a. Realtors
   b. Loan brokers
   c. Builders
   d. Architects
   e. Lumber and supply yards
   f. Prefab manufacturers
   g. Individuals
   h. Any other source of business
3. Processing for the following reasons:
   a. Familiarity with and physical closeness to locations to better know:
      (1) Neighborhood trends
      (2) Local acceptance or prejudice
      (3) Planned development not published
   b. Familiarity with the builders, promoters or sponsors to determine their qualifications as to:
      (1) Performance
      (2) Financial responsibility
   c. Physical location, i.e., close to surveyors, court house, title companies and lawyers of all parties involved.

The true success of all business from small to large depends upon sound management principles. It is not possible in an article on branch office operations to cover the entire field but some of those principles that apply to branch office operation will be cited.

It is best, as in any type of management control, to maintain the chain of command but especially so in branch operations. Branch decisions must be firmly upheld by the home office, otherwise the people dealing with them will appeal all adverse decisions and ultimately disregard the branch entirely. This will leave your company with the expense of operating a branch with few of the advantages. Even erroneous decisions should be supported as against the outsider much the same as the husband and wife "cling together" when an outsider attempts to arbitrate a family argument or "fight."

Books have been written and lifetimes have been spent in the study of management. It is recommended that management make this material and the opportunity to attend the Mortgage Bankers Association School, Courses I, II and III, available to junior personnel, both supervisory and executive. The courses are taught by mortgage banking executives selected for special ability in the subject assigned to them.

Further education in the individual's special field, whether it be accounting, appraising, or any other specialty should also be encouraged by subsidizing the educational expenses of the individuals preferably with some ratio to the degree of success, i.e., an "A" grade calling for 100 per cent company payment, "B"—90 per cent, "C"—70 per cent, balance to be paid by the individual.

Public relations type courses that achieve more diplomatic living, benefit all types of supervisory or public contacting personnel and have been employed with considerable success. In one of our own offices, such a course was arranged in cooperation with the local bank to reduce cost and furnish outside competition. Material benefits were noted even to the telephone operator, filing clerks and office supply personnel.

Problems of organization and personnel in branches are not unlike the ones existent in an operation conducted at one location. The problems are usually more severe, however, and much more acute because they are magnified by distance and time.

The work to be performed at the district or home office generally should include all that requires specialized skill and does not have to be performed at the branch. This enables the employment of much more specialized equipment and personnel, with resultant lower costs.

Banking is more satisfactorily arranged by one well qualified person at the home office acting for all branches. Consolidation of all branch escrow bank accounts into a single escrow account simplifies the bank's bookkeeping and makes for more impressive balances. This aids materially in arranging needed lines of credit at the most favorable rates and terms.

Home office operating personnel can be better qualified and specialized since for a number of offices there will be a sufficient amount of one type of work to enable a person or persons to become more proficient in the particular operation.

". . . there has been more progress made in mortgage banking operations in the past eight years than in all the prior years. To take full advantage of the technological improvements it has become necessary to add volume. Many areas in the United States have become static in population—some are even retrogressing with the availability of new mortgages dwindling. When expansion of volume could not be achieved in the existing old trade areas, branches were opened. Another reason for opening branch offices was the insistence of a mortgagee's major builder moving into an area which could not be properly served from the home office. Some builders have had projects totaling thousands of units which gave a satisfactory basis of income with which to begin operation of a branch office. Still another reason has been at the request of investors, with whom the mortgage banker has an existing contract, to cover additional territory not within the practical servicing area of the home office."

All of our branches are connected by a private telegraph system and our home office banks employ private wire systems to enable prompt cash credit to branch bank accounts promoting prompt closing of loans, a customer-satisfying procedure.

Sales of loans are best handled by the home office. Major outlets should be contacted for overall arrangements by one person authorized to commit the entire company to an agreed-upon performance. Once again a specialist can be developed by repetitive experience at the same operation. There are no firm set lines in this field in this operation since a branch that deals with one investor should do so directly. Some investors deal with two or more branches exclusively though fortunately most of our investors buy from all or almost all branches. A further advantage of branch operation is the ability of a number of branches being able to put together through home office co-ordination a sufficient amount of an investor's particular type of loans to open or maintain an account that may not otherwise be available.

Many times the availability of a standby or take-out commitment is dependent upon a large minimum and by putting together the loans of several branches, each office may qualify to do business that otherwise would be lost.

Accounting operations follow the same general principles previously cited for other types of operations. The same general truisms apply. In accounting, after the proper approach is made, the benefits seem even more apparent. Accounting, being a specialized technical subject, requires people with specialized skills. Early in our branch operation experience, each branch had its own accountant and each prepared its own operating statements and the home office merely consolidated operating statements. There was much resistance by the branch to centralizing this operation and the actual servicing accounting.

Now, it is universally recognized in the branches and the home office that it is possible to employ more capable personnel at the home office and employ only bookkeepers at the branches who feed the information to the home office. This method relieves the branch manager of most of the accounting responsibility and frees him for more productive pursuits.

Electronic equipment can be employed on all servicing. Under independent branch accounting or without the volume reached by consolidation of the work of the branch offices this would not be economically feasible. Likewise, the investor receives only one remittance statement for as wide an area as the operation covers. Where a large number of servicing agents is a problem to an investor, the mortgage banker offering service for an entire area might be granted the representation as against six or more separate companies. Even where an investor wishes to have loans in only one area the firm serves, the fact that the servicor has volume, permitting a high quality of performance for a small investor, may be the reason the account is secured.

Under the premises previously cited, all borrowers are requested to remit directly to the home office. They are encouraged to do this by furnishing them with self-addressed envelopes. These are of a special color addressed to a special post office box to achieve an automatic sort from the balance of the mail. This is from 80 to 95 per cent successful. Facilities are available at all branches to make a payment over the counter.

Customers' ledger accounts are prepared at the home office. Copies are furnished to each branch so that customers' questions may be answered on the spot. This system is highly satisfactory probably because of the private telegraph system to settle any inquiries not clear or requiring more recent figures than shown on the latest copy available at the branch.

The most controversial item in division of functions between branch and home office is undoubtedly collection procedure. After having operated both ways, it has been found to be more efficient to handle collections from a central department in the home office.

In a branch operation where the collection department is not centralized it is necessary to have the same number of departments as branches. Experience has taught the importance of having collection department personnel devote full time to collections. For example, if the collection man works part time on other activities, when they become heavy, collection follow-up is slighted, thereby violating one of the basic rules of good collection procedure, "continuous and consistent follow-up."

A company can afford to maintain a staff, trained and experienced, with the "know how" to effectively service delinquent loans, with a central collection department. The department is large enough to warrant an internal training program. Specialization makes obvious the personnel not suited to this type of employment and permits their prompt elimination. Man power being concentrated, the loss of any one man from the collection force does not severely handicap operations.

The Unit System is employed since it is the most practical method in a central collection department. Department activities are directed by a collection manager who supervises the work of unit managers assigned and responsible for all accounts in a defined territory. The unit manager follows all delinquent loans in all stages and prepares all the required reports of investors and management. The unit manager becomes familiar with the loans in his territory, able to recognize and properly handle chronic delinquents. The unit manager has field men who make both personal and telephone calls from the local branch at his direction by collection cards that are forwarded daily. The field men live in the approximate center of their territory to keep travel costs low.

Branch office operations have been found workable under the methods and patterns outlined. Perhaps this presentation does not carry conviction since it is not documented with specific citations. Representations are based on twenty years' experience in branch operations and the need is still keenly felt to improve efficiency.

Undoubtedly, branch office operations should be thoroughly studied by one of the qualified universities under the supervision of a committee of our own membership to achieve a fair and unbiased scientific analysis of this problem.

The future of mortgage banking is dependent on the improvement of its services and reduction of its costs. Major steps must be taken in this direction to preserve the mortgage banker's way of life.

In an expansion of its mortgage and real estate loan department, The First National City Bank of New York has created two new executive positions which will be filled by **Daniel G. Amend,** promoted to assistant vice president, and **Daniel D. Dickey,** assistant vice president, who has been transferred from another department.


Daniel G. Amend


Daniel D. Dickey

Mr. Amend, an experienced attorney, will handle the documentation and legal coordination of mortgage loans. Mr. Dickey, who has worked closely with correspondent banks, will assist correspondents and other customers in the financing of real estate.

Both men will be associated with **Harry A. Yoars,** vice president in charge of the department.

Brandau C. Hughes has become associated with Quigley Mortgage Service, Inc., Wilmington, Delaware, as assistant vice president.

James E. Stack has joined Percy Wilson Mortgage & Finance Corp., Chicago, as assistant manager of the corporate finance division.

For the past three years, he has been assistant appraiser in the Chicago office of the Equitable Life Assurance Society of the U. S. Previously, he was appraiser and mortgage loan negotiator with Leighly and Robertson, financial consultants. In his new position, he will handle commercial and industrial loans.

On its 25th anniversary, United Service and Research, Inc., Memphis, announced that its corporate name has been changed to **Schumacher Mortgage Company, Inc.,** in honor of its founder, the late **E. D. Schumacher,** under whose leadership the firm was built into one of the largest mortgage banking firms in the Mid-South.

The company was organized in April, 1933, by Mr. Schumacher to service real estate mortgages and properties acquired for management. A number of savings banks and insurance companies gave the company the opportunity of conducting an orderly liquidation of mortgage investments held by them. In the difficult depression years of the '30s, Mr. Schumacher and his staff performed a service for many of the farmers and other property owners by encouraging them and aiding them to save their properties. One of Mr. Schumacher's interests which aided the farmer later turned into the program, Keep Tennessee Green.

The clientele of the company has increased to include more than 50 savings banks and insurance companies in Alabama, Illinois, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Vermont and Wisconsin, with a servicing volume of over 10,000 loans.

Mr. Schumacher was the only man to serve two terms as MBA President.

Ernest P. Schumacher, son of the late Mr. Schumacher, heads the company as president.

BIGGEST YEAR YET

(Continued from page 34)

000,000 for the half year, up nearly 15 per cent. Some of this increase appears to be due to Asian flu complications, but a large part of it reflects the greater amount of protection outstanding. At this rate, the total life insurance payments for 1958 may reach $7,500,000,000.

Total funds held by the life insurance companies to guarantee this protection probably approached the $103,500,000,000 mark on June 30, a half-year rise of some $2,400,000,000. This asset increase is the result of the growing number of policies outstanding and the increasing age of those outstanding. The rise averaged about $22 per policyholder. It represents an important segment of new capital made available for the economy through the thrift of the millions of policyholders.

Adding to the new capital from asset increase, the funds becoming available for reinvestment, well over $7,500,000,000 have been invested by the U. S. life companies in the first half of 1958. The largest block of new investments was in corporate securities, primarily bonds, representing financing for business and industry. Corporate security acquisitions in the six months have totaled about $2,800,000,000. Mortgage acquisitions, chiefly new financing for residential properties, were in the neighborhood of $2,300,000,000.